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## Comments

# Reasonably Necessary Expenses or Life of Riley?: The Disposable Income Test and a Chapter 13 Debtor's Lifestyle

[I]t was not the design of the Bankruptcy laws to allow the debtor to lead the life of Riley while his creditors suffer on his behalf.<sup>1</sup>

A common perception of a debtor in bankruptcy is that of an individual who had an extravagant lifestyle and excessive expenditures that led to the need for bankruptcy relief.<sup>2</sup> The issues of lifestyle and spending habits are perhaps most relevant when a debtor proposes a plan of reorganization under Chapter 13 of the 1978 Bankruptcy Code ("Code").<sup>3</sup> Pursuant to Chapter 13, a debtor may propose a plan where the debtor keeps all property and makes specified payments from post-petition income to creditors over a three to five year period.<sup>4</sup> The debtor's income that is available to pay creditors under a

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1. *In re Bryant*, 47 Bankr. 21, 26 (Bankr. W.D.N.C. 1984). Another court expressed a similar sentiment when it stated that "a chapter 13 debtor who proposes to pay his creditors 38 cents on the dollar cannot expect to go 'first class' when 'coach' is available." *In re Kitson*, 65 Bankr. 615, 622 (Bankr. E.D.N.C. 1986).

2. For example, a commentator described this perception when he stated that "the paradigmatic bankruptcy abuser is the free-spending swinger who finances his sybaritic lifestyle at the expense of his creditors." Corish & Herbert, *The Debtor's Dilemma: Disposable Income as the Cost of Chapter 13 Discharge in Consumer Bankruptcy*, 47 LA. L. REV. 47, 69 (1987).

One court commented in regard to a debtor's spending habits that the "debtor seeks only to obtain relief from his past excesses and, given his monthly budget, obviously intends to continue the extravagant lifestyle which has brought him here in the first place." *In re Ploegert*, 93 Bankr. 641, 644 (Bankr. W.D. Ark. 1988). Another court criticized a proposed Chapter 13 plan because it "would have allowed the debtors to retain the 'spoils of their 'buying spree,'" which caused the financial crisis while the unsecured creditors would receive only 12 cents on the dollar." *In re Rice*, 72 Bankr. 311, 312 (D. Del. 1987).

3. 11 U.S.C. §§ 1301-1330 (1988).

For a good summary of the mechanics of both Chapter 7 and Chapter 13 of the Bankruptcy Code, see Breitowitz, *New Developments in Consumer Bankruptcies: Chapter 7 Dismissal on the Basis of "Substantial Abuse"*, 59 AM. BANKR. L.J. 327, 330-36 (1985); Corish & Herbert, *supra* note 2, at 52.

4. One commentator explained as follows:

Chapter 13 is roughly comparable to chapter 11, in that both govern "reorganization" bankruptcy proceedings, in which the debtor is allowed to

Chapter 13 plan is defined in the Code as "disposable income."<sup>5</sup> Disposable income consists of the debtor's net income<sup>6</sup> minus living expenses. Therefore, the amount of the payments the debtor is able to make to creditors under a Chapter 13 plan is directly related to the amount of the debtor's living expenses. Since a debtor's lifestyle dictates the amounts expended for living expenses, a debtor's lifestyle becomes an important issue in the confirmation of a Chapter 13 plan.<sup>7</sup>

The role of the bankruptcy court in scrutinizing a debtor's lifestyle before confirming a Chapter 13 plan is an unsettled issue. Because disposable income is a factor in confirming a Chapter 13 plan, the court is often required to examine the debtor's living expenses to determine whether they are "reasonably necessary."<sup>8</sup> The reasonably necessary standard raises two questions about a court's discretion in determining disposable income under a Chapter 13 plan: (1) whether the court should have such discretion, and (2) if so, how much discretion should the court be allowed? Unfettered discretion could lead to inconsistent standards and widely disparate results among the many bankruptcy jurisdictions. This disposable income issue becomes more complex in light of the objectives and policies of bankruptcy in general, and Chapter 13 in particular. For example: What standard of living should a bankruptcy court require of the debtor? What criteria should the court use in determining an acceptable standard of living? Should Congress establish objective guidelines in the interest of consistency? Should the court consider

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retain assets in exchange for payments to be made to creditors from the debtor's future income. As such, both differ from Chapter 7 "liquidation" bankruptcies, in which the debtor loses non-exempt assets but is generally freed from any further obligation to pay.

Corish & Herbert, *supra* note 2, at 48. (citations omitted).

5. 11 U.S.C. § 1325(b)(1)(B) (1988). See *infra* note 11 for the text of this Code section. The method by which a court determines the amount of a debtor's disposable income that is available to fund a Chapter 13 plan is commonly referred to as the "disposable income test." *In re Wood*, 92 Bankr. 264, 266 (Bankr. S.D. Ohio 1988).

6. A debtor's net income is often referred to as "take-home pay." The "net income" references in this Comment refer to gross wages minus any payroll deductions for such items as income taxes, FICA, and insurance.

7. After a debtor proposes a Chapter 13 plan, the court must confirm the plan for execution. For the statutory requirements for confirmation of a Chapter 13 plan, see *infra* note 12 and accompanying text.

8. Under 11 U.S.C. § 1325(b)(2) (1988), the debtor's living expenditures that are not included in disposable income must be "reasonably necessary for the maintenance or support of the debtor or a dependent of the debtor." See *infra* note 11 for the full text of this Code section. This test is referred to by courts and commentators as the "reasonably necessary" standard. See, e.g., *In re Taff*, 10 Bankr. 101, 107 (Bankr. D. Conn. 1981).

geographical differences in costs of living? These and other considerations are central to the disposable income determination: How should a court determine reasonable and necessary living expenses for the Chapter 13 debtor?

This Comment will define and analyze the issues involved in determining disposable income for the non-business Chapter 13 debtor.<sup>9</sup> It will review the statutory framework and legislative history of the disposable income test, analyze whether any trends can be discerned from the disposable income cases, and recommend an approach to the problem of calculating disposable income.

## I. STATUTORY FRAMEWORK

The starting point for the analysis of any statutory law is the statute itself. Section 1325(b) of the Code exists within the framework of Chapter 13 as a whole, and specifically, within the requirements for confirmation of a Chapter 13 plan. This section of the Comment will first examine the wording and structure of section 1325 of the Code, and then review the legislative history of section 1325(b).

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9. Chapter 13 is also available for a sole proprietor debtor. The issues, however, are slightly different. Because the majority of Chapter 13 petitions are predominately filed by non-business debtors, this Comment will focus only on the non-business context. One commentator noted that "business cases under Chapter 13 are relatively rare." Morris, *Substantive Consumer Bankruptcy Reform in the Bankruptcy Amendments Act of 1984*, 27 WM. & MARY L. REV. 91, 161 (1985).

A. Section 1325<sup>10</sup>

Section 1325(b) of the Code<sup>11</sup> defines "disposable income" as the amount of the debtor's post-petition income available to repay creditors. The section 1325(b) disposable income requirement, however, must be understood in the framework of that entire Code section. Section 1325 states the requirements for confirmation of a Chapter 13 plan. Subsection (a)<sup>12</sup> lists six

10. For a thorough discussion of the mechanics of the operation of 11 U.S.C. § 1325(b) (1988), see Butler, *A Chapter 13 Trustee Looks at Section 1325(b) of the Bankruptcy Code*, 63 AM. BANKR. L.J. 401 (1989).

11. 11 U.S.C. § 1325(b) (1988) states in full:

(1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan—

(A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or

(B) the plan provides that all of the debtor's projected disposable income to be received in the three-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

(2) For purposes of this subsection, "disposable income" means income which is received by the debtor and which is not reasonably necessary to be expended—

(A) for the maintenance or support of the debtor or a dependent of the debtor; and

(B) if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business.

*Id.*

12. 11 U.S.C. § 1325(a) (1988) states in full:

(a) Except as provided in subsection (b), the court shall confirm a plan if—

(1) the plan complies with the provisions of this chapter and with the other applicable provisions of this title;

(2) any fee, charge, or amount required under chapter 123 of title 28, or by the plan, to be paid before confirmation, has been paid;

(3) the plan has been proposed in good faith and not by any means forbidden by law;

(4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date;

(5) with respect to each allowed secured claim provided for by the plan—

(A) the holder of such claim has accepted the plan;

conditions that a Chapter 13 plan must satisfy: (1) conform to the other provisions of Chapter 13, (2) pay all priority claim amounts in full over the life of the plan, (3) be proposed in good faith (the "good faith" test),<sup>13</sup> (4) pay unsecured creditors at least as much as they would receive in a Chapter 7 liquidation (the "best interests" test),<sup>14</sup> (5) pay secured creditors the present value of their secured claims over the life of the plan, and (6) be feasible for the debtor to complete (the "feasibility" test).<sup>15</sup> If these conditions are met, the court can confirm the plan. These conditions, however, do not require payment to unsecured creditors in excess of Chapter 7 amounts, even if the debtor would be able to make larger payments. Therefore, subsection (b), the disposable income requirement, allows unsecured creditors to object to a plan that pays nominal amounts when the debtor is capable of larger payments.

Also, under section 1325(b), either the trustee or an unsecured creditor can object to confirmation of a Chapter 13 plan even though the plan satisfies the conditions of section 1325(a).<sup>16</sup> Thus, the disposable income test is not a mandatory requirement of every Chapter 13 plan. If there is an objection, however, the court may not confirm the plan unless either the plan proposes to pay the objecting claimant in full or the plan commits all of the debtor's disposable income to be received in a three-year period to the plan.<sup>17</sup> "Disposable income" is defined as income "not reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor."<sup>18</sup> Every debtor must submit a schedule of income and expenses to the court. The court is required, however, to evaluate that income and

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(B)(i) the plan provides that the holder of such claim retain the lien securing such claim; and

(ii) the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim; or

(C) the debtor surrenders the property securing such claim to such holder; and

(6) the debtor will be able to make all payments under the plan and to comply with the plan.

*Id.*

13. See *infra* note 33.

14. See *infra* note 30.

15. See *infra* note 31.

16. 11 U.S.C. § 1325(b)(1) (1988). See *supra* note 11 for the text of this Code section.

17. 11 U.S.C. § 1325(b)(1)(A) to -(B) (1988). See *supra* note 11 for the text of this Code section.

18. 11 U.S.C. § 1325(b)(2) (1988). See *supra* note 11 for the text of this Code section.

expense schedule and determine disposable income only if the trustee or an unsecured creditor objects to the confirmation of the plan.

The disposable income evaluation is a two-step process.<sup>19</sup> First, a court must determine the debtor's projected income. In this step, questions may arise about the inclusion in the debtor's projected income of overtime pay, pay raises, and a spouse's income.<sup>20</sup> Second, once the court determines the debtor's projected income, it must decide what living expenses the debtor can deduct from the projected income to arrive at the debtor's disposable income. At this point, the court must decide whether specific expenses are "reasonably necessary" to support the debtor or a dependent of the debtor. This analysis of living expenses requires the court's discretion in looking at the debtor's lifestyle. One commentator has stated that "[t]he determination of disposable income may be even more difficult than that of projected income."<sup>21</sup>

### B. Legislative History

The disposable income test was added to Chapter 13 of the Code by the Bankruptcy Amendments and Federal Judgeship Act of 1984 ("BAFJA").<sup>22</sup> The most notable thing about the legislative history of the BAFJA is its lack of history. One court stated that "the legislative history to section 1325(b) is singularly vague and unenlightening."<sup>23</sup> Many commentators, however, have examined the historical events and the House and Senate Conference Reports leading up to the passage of the BAFJA. These commentators point to three significant aspects of the history: (1) the influence of the consumer credit industry, (2) the lack of formal recorded legislative history, and (3) the

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19. 5 COLLIER ON BANKRUPTCY para. 1325.08 (15th ed. 1989). See also *In re Fries*, 68 Bankr. 676, 682 (Bankr. E.D. Pa. 1986).

20. The objective of this Comment is to focus on the second step of the analysis. For a discussion of what constitutes income for purposes of the disposable income test, see Butler, *supra* note 10, at 406-10; Corish & Herbert, *supra* note 2, at 62-68; Comment, *Section 1325(b) and Zero Payment Plans in Chapter 13*, 4 BANKR. DEV. L.J. 449, 457-63 (1987) [hereinafter Comment, *Zero Payment*].

21. Collier, *supra* note 19, at para. 1325.08. Collier explains this difficulty as follows:

As with projected income, the court, in theory, is required to project what will happen to the debtor's expenses over three years. Such a projection would require the court to guess whether the debtor would have additional children, unexpected marital separations, medical bills, home repairs, or a wide variety of other future expenses. Obviously, this is impossible.

*Id.*

22. Pub. L. No. 98-353, 98 Stat. 333 (1984).

23. *In re Jones*, 55 Bankr. 462, 465 (Bankr. D. Minn. 1985).

possibility of a congressional preference for an objective standard to determine reasonably necessary expenses.

## 1. The Influence of the Consumer Credit Industry

The consumer credit industry<sup>24</sup> played a very significant role in advising Congress on the need for changes to the 1978 Code. Although the Code was the result of many years of careful drafting,<sup>25</sup> outcries for amendment arose almost immediately. There was a general concern in the industry that debtors were abusing the purpose of bankruptcy by using the liberal provisions of the Code to avoid paying debts that they were capable of paying.<sup>26</sup> In particular, the consumer credit industry was concerned about what they perceived as excessive discharges of unsecured debt in Chapter 7 bankruptcies.<sup>27</sup> One commentator remarked that "[m]any of the consumer bankruptcy amendments were designed to rein in what some creditors saw as an excessive liberality toward debtors in the original Bankruptcy Code."<sup>28</sup>

One perceived inadequacy of the pre-BAFJA Code was that it did not require a Chapter 13 plan to pay general unsecured creditors any greater

24. Although no single group officially represents the entire consumer credit industry, the legislative hearings in conjunction with the BAFJA heard testimony from a number of groups. These groups included the Credit Union National Association, the National Association of Federal Credit Unions, the National Consumer Finance Association, the American Retail Federation, and the National Retail Merchants Association. Gross, *Preserving a Fresh Start for the Individual Debtor: The Case for Narrow Construction of the Consumer Credit Amendments*, 135 U. PA. L. REV. 59, 61 n.4 (1986).

25. One commentator stated that the Code "resulted from nearly a decade of study and drafting." Morris, *supra* note 9, at 94.

26. A commentator summarized some excerpted comments symbolizing this credit industry attitude:

*Bankruptcy Reform Act of 1978: Hearings Before the Subcomm. on Courts of the Senate Comm. on the Judiciary*, 97th Cong., 1st Sess. 6, 37 (1981) . . . ("[I]t appears that consumers may be taking advantage of the liberalized law to escape burdens which could be assumed and which need not necessarily lead to bankruptcy."); . . . 130 CONG. REC. H7497 (daily ed. June 29, 1984) (Congressman Brooks, speaking on the proposed bankruptcy reforms, stated: "This bill will also make personal bankruptcy reforms by eliminating the use of the bankruptcy system by debtors who are not suffering economic hardship."). . . .

Gross, *supra* note 24, at 61 n.5.

27. The Eighth Circuit noted that the amendments were passed in response to an increasing number of Chapter 7 bankruptcies each year by non-needy debtors. *In re Walton*, 866 F.2d 981, 983 (8th Cir. 1989).

28. Corish & Herbert, *supra* note 2, at 47-48.



amounts than they would have received in a Chapter 7 liquidation.<sup>29</sup> The "best interest" test of section 1325(a)(4)<sup>30</sup> established a minimum standard for payment to general unsecured creditors under a Chapter 13 plan, but the pre-BAFJA Code set no maximum standard for payment to them. Without a maximum standard in the pre-BAFJA Code, the courts used one or more of the so-called "feasibility test,"<sup>31</sup> "best interest test,"<sup>32</sup> or "good faith test"<sup>33</sup> to determine whether a Chapter 13 plan proposed to pay enough to the unsecured creditors. The result was a very wide discrepancy among the different bankruptcy districts.<sup>34</sup> Some courts confirmed plans that paid as

29. One commentator has written that "the major problem with section 1325 [of the Code] was the absence of a meaningful standard for determining what portion of the debtor's income he should devote to the plan." Comment, *The Religious Debtor's Conviction To Tithe as the Price of a Chapter 13 Discharge*, 66 TEX. L. REV. 873, 876 (1988) [hereinafter Comment, *Religious Debtor's*].

30. For the full text of 11 U.S.C. § 1325(a)(4) (1988), see *supra* note 12. Based on this subsection, the debtor must propose in their Chapter 13 plan to pay unsecured creditors at least as much as they would have received had the debtor liquidated under a Chapter 7 bankruptcy. *Educ. Assistance Corp. v. Zellner*, 827 F.2d 1222, 1224 (8th Cir. 1987) ("Under the 'best interests of creditors' test of Chapter 13, a plan should not be confirmed if the property to be distributed under the plan is less than the amount each allowed unsecured creditor would be paid if the debtor's estate were liquidated under Chapter 7.").

31. For the full text of 11 U.S.C. § 1325(a)(6) (1988), see *supra* note 12. Based on this subsection, the bankruptcy court has the authority to refuse to confirm a plan if the court, in its discretion, determines that the debtor will not reasonably be able to make payments for the term of the plan. Prior to the BAFJA, however, some bankruptcy courts interpreted this section to allow them to deny confirmation of a Chapter 13 plan because the debtor could feasibly pay a greater dividend to the general unsecured creditors.

32. See *supra* note 30.

33. For the full text of 11 U.S.C. § 1325(a)(3) (1988), see *supra* note 12. This is a very broad and discretionary bankruptcy provision that allows a bankruptcy court to deny confirmation of a Chapter 13 plan if, under the totality of the circumstances, the court determines that the debtor has not proposed the plan in good faith. This section became the most widely used by the courts to increase the dividend to the general unsecured creditors under Chapter 13 plans. Some courts would refuse to confirm a Chapter 13 plan that proposed a nominal payment to the unsecured creditors because the plan was not proposed in good faith in that the debtor could pay more. One court stated that "prior to passage of the Bankruptcy and Federal Judgeship Act of 1984 ("BAFJA"), many courts used the so-called 'good faith test' to compel a minimum repayment as a condition of confirmation." *In re Pierce*, 82 Bankr. 874, 878 (Bankr. S.D. Ohio 1987).

34. One court noted that 11 U.S.C. § 1325(b) (1988) was added "in response to the divergence of opinion among the courts as to the minimum level of payment

little as one percent to the general unsecured creditors, while other courts required a substantial percentage repayment before they would confirm a Chapter 13 plan.<sup>35</sup>

The consumer credit industry believed that the pre-BAFJA Code favored debtors in two principal ways. First, they believed that consumers with few assets and large incomes<sup>36</sup> were choosing to discharge debts under a Chapter 7 liquidation rather than to reorganize and repay creditors in a Chapter 13 plan.<sup>37</sup> This perceived abuse was possible because Chapter 13 was completely voluntary. The courts, absent an application of a test such as "good faith,"<sup>38</sup> could not force debtors to file under Chapter 13 merely because the debtors had the income potential to repay a substantial percentage of their debts to general unsecured creditors. Thus, there was a concern that debtors with the "ability to pay" in a Chapter 13 reorganization were opting instead for a broad debt discharge under a Chapter 7 liquidation.<sup>39</sup> Second, the industry believed that Chapter 13 allowed for "cheap" reorganizations, because there was no requirement that the amount paid to unsecured creditors exceed what they would have received in a Chapter 7 liquidation.<sup>40</sup> Debtors with

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necessary to meet the good faith requirement of Section 1325(a)(3)." *In re Reyes*, 106 Bankr. 155, 158 (Bankr. N.D. Ill. 1989).

35. One commentator stated as follows:

Both creditors and debtors reacted to these divergent interpretations of the confirmation requirements [of section 1325 of the Code] by calling for a more defined standard. Creditors wanted a standard that would ensure meaningful repayments on unsecured obligations. Debtors sought a standard that would not prohibit them from using Chapter 13 simply because they were too poor to repay a set percentage of their unsecured debts after considering their necessary financial obligations.

Comment, *Religious Debtor's*, *supra* note 29, at 877-78.

36. For a more thorough discussion of the high income/low asset debtor issue, *see* Corish & Herbert, *supra* note 2, at 81-82.

37. One commentator stated that the unsecured creditors criticized the Code in that "it was 'too easy' to file for liquidation under Chapter 7; too many people who 'could pay' were liquidating just to 'shuck a couple of debts.'" Corish & Herbert, *supra* note 2, at 54 (citing *In re Bryant*, 47 Bankr. 21, 24 (Bankr. W.D.N.C. 1984)).

38. *See supra* note 33.

39. *See In re White*, 49 Bankr. 869, 872 (Bankr. W.D.N.C. 1985) ("The consumer credit amendments . . . were the offspring of congressional concern that credit costs were being driven upwards by the ready availability of discharge via Chapter 7 to persons seeking to sidestep consumer credit obligations who had the ability to pay.").

40. A commentator writing shortly after the passage of the BAFJA stated that "while historically bankruptcy originated as a means to insure the equitable distribution of a debtor's assets where those assets were insufficient to pay such debtor's debts in full, it has presently evolved into a method of escaping those debts at little or no sacrifice." Breitowitz, *supra* note 3, at 327-28 (citations omitted).

small incomes and many assets could retain assets in a Chapter 13 reorganization with a minimal repayment to general unsecured creditors, because the debtors had little income to devote to the plan. Thus, the consumer credit industry believed that debtors were choosing either to propose Chapter 13 plans that paid very little to the general unsecured creditors, or to discharge the general unsecured debt in Chapter 7 liquidations. Under either scenario, the industry believed that the pre-BAFJA Code did not give general unsecured creditors much return on their claims and that it was weighted in favor of debtors.

As a result, the consumer credit industry began to lobby heavily for changes in the Code. The industry gathered bankruptcy statistics to reinforce their recommendations.<sup>41</sup> One industry recommendation was that "to obtain a discharge, all consumer debtors who had disposable income be required to pay their creditors all of their income in excess of a somewhat adjusted version of the federal poverty level for a period of several years."<sup>42</sup> This recommendation represented the two general industry goals for bankruptcy reform. First, debtors with incomes sufficient to pay more than a minimal percentage to general unsecured creditors under a Chapter 13 plan should be forced to reorganize under Chapter 13.<sup>43</sup> Second, the lifestyle of a Chapter 13 debtor should be reduced to a level only slightly above the recognized poverty level in order to maximize the amount of income available to repay unsecured creditors.<sup>44</sup>

## 2. Formal Legislative History

As already noted, the formal legislative history for the section 1325(b) disposable income test is almost nonexistent.<sup>45</sup> One commentator noted that "[t]he so-called Conference Report contains nothing more than the text of the corrected bill that ultimately became law."<sup>46</sup> Prior to BAFJA, two Congressional bills had proposed changes in the requirements for Chapter 13 plan confirmation. Although never enacted, the bills did include some discussions recorded in their formal legislative histories. In December of 1981, S. 2000

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41. The most significant and most quoted study was one conducted by the business school at the University of Purdue often referred to as the "Purdue Study." CREDIT RESEARCH CENTER, KRANNERT SCHOOL OF MANAGEMENT, PURDUE UNIVERSITY, MONOGRAPHS NO. 23-24, CONSUMER BANKRUPTCY STUDY (1982).

42. Corish & Herbert, *supra* note 2, at 54 (citation omitted).

43. *Id.* at 74.

44. *Id.*

45. For a thorough discussion of the legislative history of the BAFJA, see Gross, *supra* note 24.

46. Breitowitz, *supra* note 3, at 336 (citation omitted).

was introduced in the 97th Congress. The bill proposed that a debtor would not be permitted to file under Chapter 7 if "he could pay a reasonable portion of his prepetition debts out of anticipated future income."<sup>47</sup> The Senate Report for S. 2000 indicated that a 75% repayment of non-mortgage debt would be presumed a "reasonable portion" and a 25% repayment would be presumed unreasonable.<sup>48</sup> The bill would have given the bankruptcy court discretion to determine whether an amount between 25% and 75% was a reasonable repayment of non-mortgage debt.<sup>49</sup> No action was taken on S. 2000 in the 97th Congress, so it was reintroduced as S. 445 in the 98th Congress. In response to criticism that the "anticipated future income" test of S. 2000 would not work, an amendment replaced that test with the "substantial abuse" test for dismissal of a Chapter 7 liquidation proceeding.<sup>50</sup> Congress, however, did not pass S. 445.

The real impetus for amendment to the Chapter 13 plan confirmation portion of the Code came from the Supreme Court's decision in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*<sup>51</sup> In *Marathon*, the Court held that the expanded jurisdiction given federal bankruptcy courts under the Code was unconstitutional.<sup>52</sup> The Court stayed, however, the effect of its decision until December 1982, to give Congress time to revise the bankruptcy court system.<sup>53</sup> Thus, the need to quickly reform the bankruptcy court system, together with the lobbying efforts of the consumer credit industry, led Congress to hastily adopt BAFJA without much formal legislative history.<sup>54</sup> "Basically, Congress adopted the proposals of the National Bankruptcy Conference"<sup>55</sup> as the BAFJA amendments to Chapter 13 of the Code.

47. *Id.* at 345.

48. *Id.*

49. *Id.*

50. *Id.* at 346.

51. 458 U.S. 50 (1982).

52. *Id.* at 87.

53. *Id.* at 88; *United States v. Marathon Pipe Line Co.*, 459 U.S. 1094 (1982).

54. One commentator noted that "Congress was in such a hurry to adopt H.R. 5174, the BAFJA bill, that it failed to provide any official legislative reports explaining the new law." Comment, *Religious Debtor's*, *supra* note 29, at 875 (citations omitted). See also *In re Busbin*, 95 Bankr. 240, 243 (Bankr. N.D. Ga. 1989) ("amidst the frenetic legislating in 1984 to amend the Bankruptcy Code to overcome the constitutional defect identified in [*Northern Pipeline*] . . . , Congress passed the Consumer Credit Amendments . . .").

55. Comment, *The Disposable Income Test: An Attempt Toward Uniformity*, 4 BANKR. DEV. J. 221, 222 (1987) [hereinafter Comment, *Disposable Income*].

Under BAFJA, the consumer credit industry succeeded in getting sections 707(b)<sup>56</sup> and 1325(b)<sup>57</sup> added to the Code.<sup>58</sup> Section 707(b) allows a court to dismiss a Chapter 7 liquidation proceeding *sua sponte* if a discharge would be a "substantial abuse" of Chapter 7.<sup>59</sup> The credit industry hoped that this "substantial abuse" test would allow bankruptcy courts to deny liquidation treatment to a debtor who had stable income and few assets that would be liquidated in a Chapter 7, thereby reducing the number of debtors who were using bankruptcy to avoid paying creditors in a Chapter 13 reorganization. Section 1325(b) added the disposable income requirement. The credit industry believed this requirement would force debtors in a Chapter 13 reorganization to commit more than a nominal amount of their income to the plan.<sup>60</sup> The

56. 11 U.S.C. § 707(b) (1988) states in full:

After notice and a hearing, the court, on its own motion or on a motion by the United States Trustee, but not at the request or suggestion of any party in interest, may dismiss a case filed by an individual debtor under this chapter whose debts are primarily consumer debts if it finds that the granting of relief would be a substantial abuse of the provisions of this chapter. There shall be a presumption in favor of granting the relief requested by the debtor.

*Id.*

57. For the text of this section, see *supra* note 11.

58. "Congress adopted many of the credit industry's proposed reforms in 1984 when it passed the Bankruptcy Amendments and Federal Judgeship Act of 1984." Morris, *supra* note 9, at 95. Another commentator has maintained that "the confluence of a disastrous economy, a conservative political environment, and pressure created by two Supreme Court decisions, together with some legitimate creditor concerns over the operation of the Code, assisted the credit industry in successfully lobbying for major changes in the treatment of individual debtors." Gross, *supra* note 24, at 82. See also Corish & Herbert, *supra* note 2, at 55.

59. Corish & Herbert, *supra* note 2, at 55.

60. One commentator stated as follows:

Largely known as the 'ability-to-pay test,' Section 1325(b) was adopted by Congress almost verbatim from a proposal made by the National Bankruptcy Conference ("NBC") at Hearings Before the Judiciary Committee. The NBC urged that debtors only be allowed to avail themselves of the liberal provisions of Chapter 13 if they pay creditors what they are reasonably able to pay from their future income. According to the NBC, correlating a debtor's right to Chapter 13 relief to his ability to pay from future disposable income made sense because most unsecured credit was actually extended based on the debtor's ability to pay from future income.

Comment, *Zero Payment*, *supra* note 20, at 455 (citations omitted).

One court stated that "[t]his modification [11 U.S.C. § 1325(b) (1988)] came into being because of the reaction of Congress to perceived abuses in Chapter 13 plans and more particularly the so-called 'zero payment' and minimal payment plans." *In re*

disposable income test was intended, at least in part, to increase the dividend to unsecured creditors, and is often referred to as the ability-to-pay test.<sup>61</sup>

### 3. The Congressional Reference to Department of Labor Statistics

Due to a lack of formal legislative history for BAFJA, bankruptcy courts have debated whether Congress intended courts to use an objective standard to determine reasonably necessary expenses under the disposable income test. The courts have interpreted the disposable income test as a congressional attempt to settle the issue of how much income a Chapter 13 debtor must commit to his Chapter 13 reorganization plan.<sup>62</sup> One court noted that "the new subsection [1325(b)] incorporates into chapter 13 the 'ability to pay' test, which requires debtors to pay as much as they are able, but only as much as they are able."<sup>63</sup> That court noted that the history of the disposable income test presumes "'a substantial effort by the debtor to pay his debts', and furthermore, '[s]uch an effort may require some sacrifices by the debtor.'"<sup>64</sup>

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Tracey, 66 Bankr. 63, 66 (Bankr. D. Md. 1986).

61. In adopting 11 U.S.C. § 1325(b) (1988), Congress noted that "the present proposal is that the ability-to-pay test, once invoked by the holder of an allowed unsecured claim, should serve as the standard for determining whether the debtor is reasonably capable of *paying more* than originally proposed." *Personal Bankruptcy: Oversight Hearings Before the Subcommittee on Monopolies and Commercial Law of the House Committee on the Judiciary*, 97th Cong., 1st and 2d Sess. 213 (1981-82). One court stated that "[t]his new provision [Section 1325(b)] is referred to as the 'ability to pay' or 'disposable income' test." *In re Ashton*, 85 Bankr. 766, 768 (Bankr. S.D. Ohio 1988) (citation omitted).

62. "11 U.S.C. § 1325(b) represents Congress' attempt to statutorily resolve issues relating to the appropriate minimum requirements for funding a chapter 13 plan from a debtor's postpetition income." *In re Navarro*, 83 Bankr. 348, 354 (Bankr. E.D. Pa. 1988) (citations omitted). Prior to BAFJA, the courts had debated whether a nominal or zero-payment plan would pass a good faith test. See Comment, *Zero Payment*, *supra* note 20.

63. *In re Jones*, 55 Bankr. 462, 465 (Bankr. D. Minn. 1985).

64. *Id.* (quoting S. Rep. No. 65, 98th Cong. 1st Sess. 22 (1983)). See also *In re Navarro*, 83 Bankr. 348, 354 (Bankr. E.D. Pa. 1988) (citing S. Rep. No. 65, 98th Cong. 1st Sess. 22 (1983)).

The *Navarro* court also commented as follows: Chapter 13 relief is essentially equitable, and contemplates a substantial effort by the debtor to pay his debts. Such an effort, by definition, may require some sacrifices by the debtor, and some alteration in prepetition consumption levels. Thus, the debtor might reasonably be required to devote to the plan that portion of his income which is not necessary for support of the debtor and his family. The courts may be expected to determine norms for such support, and Labor Department cost of living figures may provide some help. This approach will also permit plans to be confirmed where the debtor does make a

The courts have been unable to decide, however, whether Congress intended the use of an objective standard to determine necessary expenses. This uncertainty regarding congressional purpose has produced inconsistency among the bankruptcy jurisdictions.

The issue regarding objective criteria for determining reasonable expenses is further complicated because Congress made a reference to the Department of Labor cost of living statistics as the standard for determining whether the debtor's expenses during the Chapter 13 plan are reasonable.<sup>65</sup> This reference to the Department of Labor statistics has been interpreted by a few courts and commentators to mean that Congress intended some sort of base line average standard to be applied when analyzing living expenses for a Chapter 13 plan.<sup>66</sup> The bankruptcy courts, however, have not adopted objective criteria to evaluate the reasonableness of the debtor's living expenses under a Chapter 13 plan. Perhaps Congress' refusal to clarify what it meant by "reasonably necessary" is an indication that Congress intended the courts to use discretion in evaluating expenses under a Chapter 13 plan.<sup>67</sup> It is also significant that Congress did not adopt the consumer credit industry's recommendations of either a poverty level standard of living for a Chapter 13 debtor or a forced Chapter 13 reorganization.<sup>68</sup> By failing to require specific levels of expenditure or mandatory Chapter 13 for certain types of debtors, Congress may have been expressing a desire to allow bankruptcy courts to evaluate expenses on a case-by-case basis.

## II. CASE LAW

Bankruptcy courts have been forced to consider "what standard is to be applied in determining the portion of a debtor's income that is not reasonably necessary for the maintenance or support of the debtor or the debtor's dependents"<sup>69</sup> because the legislative history for the disposable income test

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substantial effort to pay his debts, even though the payment itself is not substantial.). *Navarro*, 83 Bankr. at 354 (citation omitted).

65. S. REP. NO. 65, 98th Cong., 1st Sess. 22 (1983).

66. See, e.g., *In re Fries*, 68 Bankr. 676, 683 (Bankr. E.D. Pa. 1986).

67. One commentator stated that "the inherent ambiguity in the definition of disposable income allows judges to tailor the repayment plan to the circumstances of each debtor." Comment, *Religious Debtor's*, *supra* note 29, at 882 (citation omitted).

68. Following a discussion of the credit industry's suggestions to Congress for changes to the Code, one commentator stated that "[i]n the end, the concepts of forced reorganization and mandatory payment standards were largely rejected." Corish & Herbert, *supra* note 2, at 55.

69. *In re Jones*, 55 Bankr. 462, 465 (Bankr. D. Minn. 1985).

is both vague and unenlightening.<sup>70</sup> Courts will often discuss the disposable income test in determining whether a Chapter 7 case should be dismissed as "substantial abuse"<sup>71</sup> or whether a Chapter 13 case has been proposed in "good faith."<sup>72</sup> Whatever the context, bankruptcy courts evaluating proposed Chapter 13 expenditures for reasonableness under the disposable income test have used one of three approaches to reach the determination.

At one extreme,<sup>73</sup> some courts take the position that only luxury items should be disallowed as unnecessary expenses.<sup>74</sup> Under this approach, the court reviews the debtor's schedule of expenses and is concerned only when there are luxury expenditures in the budget. Probably the best expression of this approach is the often quoted language from the leading commentary on the Code:

Hence, a court determining the debtor's disposable income is not expected to, and should not, mandate drastic changes in the debtor's lifestyle to fit some preconceived norm for chapter 13 debtors. The debtor's expenses should be scrutinized only for luxuries which are not enjoyed by an average American family. . . . Indeed, where a debtor's total household income is only a modest amount, the court should be reluctant to impose its own values with respect to any expenditures, even those which seem unnecessary; the debtor's choice to make such expenditures rather than spending a greater amount on, for example, housing or clothing expenses which the court would find reasonable, is not one with which the court should interfere.

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70. One commentator remarked that "[n]either the Bankruptcy Code nor the legislative history of the Bankruptcy Amendments Act provides any significant guidance to the bankruptcy courts concerning the reasonableness issue." Morris, *supra* note 9, at 157. See also Collier, *supra* note 19, at para. 1325.08 ("[t]he legislative history gives little guidance as to what is meant by this term [reasonably necessary].").

71. One court noted the following:

The disposable income inquiry conducted in reviewing Chapter 13 petitions under Code § 1325(b) is similar to that used to review Chapter 7 petitions for substantial abuse under Code § 707(b). This is because one of the determinations to be made in a Chapter 7 substantial abuse review is whether the petition might be better filed under Chapter 13 or Chapter 11. "The primary factor that may indicate a substantial abuse is the ability of the debtor to repay the debts out of future disposable income." (footnote omitted).

*In re Sutliff*, 79 Bankr. 151, 158 (Bankr. N.D.N.Y. 1987) (citations omitted).

72. *In re Little*, 116 Bankr. 615, 618-20 (Bankr. S.D. Ohio 1990).

73. One commentator noted that this approach has not been widely adopted by the courts. Comment, *Disposable Income*, *supra* note 55, at 230.

74. One commentator referred to this approach as being "discharge oriented." Corish & Herbert, *supra* note 2, at 61.



In short, the court cannot and should not order debtors to alter their lifestyles where there is no obvious indulgence in luxuries, even where one or more unsecured creditors demand such a change. To engage in such close judgments and supervision would be to contravene the intent of Congress. It would also place impossible burdens on the court in determining the absolute necessity of every expense in each debtor's budget. Since the views of judges on such value-laden issues differ significantly, such an interpretation of the amendments would contravene their purpose of restoring nationwide uniformity to chapter 13.<sup>75</sup>

Thus, this approach maintains that a court should not impose its values on the debtor except in cases of obvious luxuries or extravagance.<sup>76</sup> This is often referred to as the "narrow"<sup>77</sup> interpretation of disposable income because it is based on the discretion of the debtor, with minimal restraint from the court.<sup>78</sup>

A second approach, known as the "broad" interpretation,<sup>79</sup> takes the opposite extreme. Courts advocating this position state that they should use broad discretion and impose their values on the debtor's budget to ensure the debtor is only proposing expenses for life's basic necessities.<sup>80</sup> The objective is for the court to examine every expense category to eliminate any expenditure that is not absolutely necessary for the support and maintenance of the debtor or his dependents. The premise is that the debtor should be reduced to a basic lifestyle to minimize expenses and thereby maximize the amount of disposable income available to pay general unsecured creditors.<sup>81</sup> This is the

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75. Collier, *supra* note 19, at § 1325.08.

76. "In general, 11 U.S.C. § 1325(b) should not be considered a mandate for a court to superimpose its values and substitute its judgment for those of the debtor on basic choices about appropriate maintenance and support." *In re Navarro*, 83 Bankr. 348, 355 (Bankr. E.D. Pa. 1988) (footnote omitted).

77. *Id.*

78. For a more thorough discussion of this approach, see Gross, *supra* note 24, at 130-40.

79. *Id.* at 122-30.

80. "Several courts have interpreted the reasonably necessary standard to include only those expenses for basic needs not related to the debtor's former status in society or lifestyle to which he is accustomed." *In re Reyes*, 106 Bankr. 155, 157 (Bankr. N.D. Ill. 1989). One commentator explained this approach by stating that it permits "a court to substitute its own judgment for that of the debtor as to the propriety of the type and amount of the debtor's expenditures." Morris, *supra* note 9, at 122.

81. One commentator characterized this approach as being "collection oriented." Corish & Herbert, *supra* note 2, at 61.

approach adopted by a majority of the courts that have considered the reasonableness of a debtor's expenditures in a Chapter 13 plan.<sup>82</sup>

The leading case advocating the broad interpretation, *In re Jones*,<sup>83</sup> was the first attempt by a court to address the disposable income test after the effective date of BAFJA. The court turned to section 522(d)(10)(E) of the Code for guidance in defining reasonably necessary expenses.<sup>84</sup> That section exempts from the bankruptcy estate certain benefit payments made to the debtor, such as pension plan assets, "to the extent reasonably necessary for the support of the debtor and any dependents of the debtor."<sup>85</sup> The *Jones* court noted that the "reasonably necessary" standard was first interpreted in *In re Taff*<sup>86</sup> as standing for the proposition that "the appropriate amount to be set aside for the debtor ought to be sufficient to sustain basic needs not related to [the debtor's] former status in society or the life style [sic] to which he is accustomed."<sup>87</sup> The court then stated that "the purpose of chapter 13 is to provide the maximum recovery to creditors while at the same time leaving the debtor sufficient money to pay for his or her basic living expenses."<sup>88</sup> According to this standard, as enunciated in *Jones*, a court should eliminate any expense not necessary for basic living and reduce any expense that is in excess of the average lifestyle. This approach does not give any weight to the debtor's former standard of living; rather, it seeks to maximize the dividend for general unsecured creditors.

A third approach takes the middle ground. Courts advocating this approach treat the disposable income test as a factual determination that varies debtor-by-debtor and case-by-case.<sup>89</sup> This approach is most appropriately characterized as the "totality of the circumstances" approach.<sup>90</sup> Courts using

82. See Comment, *Disposable Income*, *supra* note 55, at 230.

83. 55 Bankr. 462 (Bankr. D. Minn. 1985).

84. *Id.* at 466.

85. 11 U.S.C. § 522(d)(10)(E) (1988).

86. 10 Bankr. 101 (Bankr. D. Conn. 1981).

87. *Jones*, 59 Bankr. at 466.

88. *Id.*

89. One commentator explained the following:

[t]he proper amount for an expense that satisfies a basic need 'is a fact question that must be determined in the individual context of each debtor and his dependents,' taking into consideration the economic conditions in the debtor's geographic area and the amount that an average family in similar circumstances might reasonably expect to spend in order to maintain a reasonable standard of living.

Comment, *Religious Debtor's*, *supra* note 29, at 886 (quoting *In re Sutcliffe*, 79 Bankr. 151, 158 (Bankr. N.D.N.Y. 1987).

90. "What is reasonably necessary is a question of fact and depends on the totality of circumstances of the individual debtor's case." *In re Bien*, 95 Bankr. 281, 283

this totality-of-the-circumstances approach focus on the debtor's behavior in proposing the plan, past spending habits and desire to repay creditors.<sup>91</sup> This approach is a compromise between the other two extremes and it is relatively recent in its development.<sup>92</sup> In effect, it is somewhat of an equitable approach to the "reasonably necessary" determination.<sup>93</sup>

The objective is to examine each expense category on its own merits and allow the debtor some semblance of his regular lifestyle within the confines of the average lifestyle in the debtor's geographical area.<sup>94</sup> For example, in an analysis of proposed recreation expenses in a Chapter 13 plan, one court stated that "the amount of recreation in each Chapter 13 budget is a fact question that must be determined in the individual context of each debtor and his dependents."<sup>95</sup> One court proposed the following set of factors for consideration when using the totality of the circumstances approach:

While a court should not lightly substitute its judgment for that of the debtor, section 1325(b) mandates that it do so when any one of the following factors is present:

- a. the debtor proposes to use income for luxury goods or services;
- b. the debtor proposes to commit a clearly excessive amount to non-luxury goods or services;
- c. the debtor proposes to retain a clearly excessive amount of income for discretionary purposes;

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(Bankr. D. Conn. 1989). Another court stated the following: "[w]hen a determination of disposable income is presented to the Court as a contested matter, each case must be examined upon the evidence presented. The Court will determine under the totality of the circumstances whether the debtor's expenses were reasonably necessary for family support."

*In re Kuhlman*, 118 Bankr. 731, 739 (Bankr. D.S.D. 1990).

91. See, e.g., *In re Reyes*, 106 Bankr. 155, 157 (Bankr. N.D. Ill. 1989) ("The Debtor's proposal to continue his indifference, or lack of commitment, to creditors through a Chapter 13 does, however, violate the disposable income requirement.").

92. As an example of this approach, one court reasoned that although "there are some monthly expenditures quite out-of-line for the norm, . . . [t]he basic factual issue . . . is whether the *total picture* is abusive." *Waites v. Braley*, 110 Bankr. 211, 215 (E.D. Va. 1990) (court's emphasis).

93. "These judgments are guided by the court's sense of equity, which lies at the foundation of all bankruptcy law." *In re Sutliff*, 79 Bankr. 151, 157 (Bankr. N.D.N.Y. 1987).

94. For example, in an analysis of recreation expenses proposed in a Chapter 13 plan, one court stated that the proposed amount in this case (more than six and one-half percent of the debtor's net income) was "a high and unreasonable sum for entertainment, in light of Debtor's single marital status and the regional cost of living in the area where he resides." *Id.* at 158.

95. *Id.*

- d. the debtor proposes expenditures which would not be made but for a desire to avoid payments to unsecured creditors;
- e. the debtor's proposed expenditures as a whole appear to be deliberately inflated and unreasonable.<sup>96</sup>

These factors are an example of a court attempting to combine flexibility based on an individual debtor's situation, together with certain outer parameters that are assumed to govern all reasonable debtor expenditures.

In reality, the reasonably necessary determination for Chapter 13 proposed expenditures is a two-step analysis. First, in the "qualitative" step, the court must determine whether the expense itself is necessary for the support of the debtor and his dependents. In this step, the court must determine what types of expense categories will be allowed as reasonable living expenses in a Chapter 13 plan. Second, in the "quantitative" step, once an expense category is determined to be necessary, the court must decide how much the debtor may expend within the category. In this step, the court must examine a debtor's Chapter 13 budget to make sure the amount proposed to be spent in a reasonable category of expenditure is a reasonable amount.

The cases since BAFJA have developed certain categories of expenses that the bankruptcy courts consider reasonably necessary. Also, these same cases generally discuss the amount of expenditure within each expense category that the court will approve as reasonable. Thus, the cases provide a basis to examine whether the courts have established any definable standards for lifestyle expenditures in a debtor's Chapter 13 plan. The following is an analysis of the categories and amounts discussed by the courts in the context of disposable income determinations.<sup>97</sup>

### A. *Housing: Amounts Held Reasonable*

The amount that a debtor expends on housing is, perhaps, the most difficult category of expenditure to analyze and to set any meaningful objective standard for measuring reasonableness. Housing costs are extremely

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96. *In re Navarro*, 83 Bankr. 348, 355-56 (Bankr. E.D. Pa. 1988) (citations omitted). The court noted that "[t]hese factors are not meant to be exclusive, but rather a guide to relevant considerations in evaluating a case under section 1325(b)." *Id.* at 355 n.11.

97. All the cases examined specifically discuss disposable income and reasonably necessary expenses. Many of the cases, however, are actually determinations of good faith or substantial abuse. Because the courts often consider disposable income relevant to a determination of substantial abuse or good faith, they will discuss the debtor's ability to pay under a Chapter 13 plan in light of the debtor's submitted budget. The discussion of the debtor's ability to pay necessitates an analysis of the debtor's income and reasonably necessary living expenses.

sensitive to location, both geographically around the country and within a particular city.<sup>98</sup> Also, the neighborhood where a family chooses to live is often dictated by such considerations as proximity to work and quality of the school district.<sup>99</sup> Consequently, the bankruptcy courts very seldom refuse to confirm a plan because of the amount a debtor is expending for housing. For example, one court considered a \$1433 per month home mortgage reasonable for a family of five,<sup>100</sup> and another court held that \$1255 per month for a house payment and \$241 per month for utilities for a family of four was reasonably necessary.<sup>101</sup> The same is true for debtors who rent. The courts almost never refuse to confirm a plan because of unreasonable expenditures for rent. For example, one court held that a rent and utilities payment of

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98. Corporations experience this cost differential when they transfer employees from one area of the country to another. Often, corporations must pay salary differentials because housing costs vary so much among the different regions of the country. For example, expenditures for housing generally are much less in the Midwest than either Los Angeles or New York City.

99. "The debtor also may have a legitimate interest in staying in a particular location to obtain noneconomic benefits such as a superior school system." Morris, *supra* note 9, at 159.

100. *In re Stein*, 91 Bankr. 796, 803 n.2 (Bankr. S.D. Ohio 1988). The court refused to confirm the plan because of excessive food and transportation expenses but did not deem the housing expenditure to be excessive. *Id.* at 802-03. The debtor's plan proposed a 10% dividend to general unsecured creditors. *Id.* at 797.

101. *In re Greer*, 60 Bankr. 547, 549 (Bankr. C.D. Cal. 1986). It is important to note that the case was in California and that housing costs in that state are among the highest in the nation. The expenditure was considered reasonable even though the plan proposed a 1% dividend to general unsecured creditors. *Id.* at 549.

Other examples of expenditures for home mortgages held reasonable by the courts include: *In re Killough*, 900 F.2d 61, 62 (5th Cir. 1990) (\$262.07 per month for a family of two); *In re Gyurci*, 95 Bankr. 639, 640 (Bankr. D. Minn. 1989) (\$810 per month for a family of five); *In re Sustek*, No. 87-03864, slip op. at 5 (Bankr. D.S.C. March 29, 1988) (\$1,487); *In re Wood*, 92 Bankr. 264, 266 (Bankr. S.D. Ohio 1988) (\$1,004 per month for a family of three); *In re Easley*, 72 Bankr. 948, 949 (Bankr. M.D. Tenn. 1987) (\$321 per month for a single debtor); *In re Rogers*, 65 Bankr. 1018, 1022 (Bankr. E.D. Mich. 1986) (\$522.58 per month for a single debtor, including \$324 for a first mortgage and \$198.58 for a second); *In re Fries*, 68 Bankr. 679 (Bankr. E.D. Pa. 1986) (\$1,000 per month for a family of five); *In re Walton*, 69 Bankr. 150, 152 (Bankr. E.D. Mo. 1986), *aff'd*, 866 F.2d 981 (1989) (\$350 per month for a family of four); *In re Grant*, 51 Bankr. 385, 395 (Bankr. N.D. Ohio 1985) (\$900 per month for a family of four); *In re Schyma*, 68 Bankr. 52, 57 (Bankr. D. Minn. 1985) (\$552 per month for a family seven); *In re Bryant*, 47 Bankr. 21, 24 (Bankr. W.D.N.C. 1984) (\$671 per month for a family of four).

\$350 per month for a single debtor was reasonable even though the debtor paid it to her father.<sup>102</sup>

The bankruptcy courts can, however, hold extravagant or luxurious expenditures for housing to be unreasonable. For example, in *In re Krohn*,<sup>103</sup> subsequent to a Chapter 7 petition, the debtors sold a \$98,500 condominium and reinvested the \$19,701 gain in a new \$156,000 residence.<sup>104</sup> Although it was not a Chapter 13 disposable income case, the court commented that the debtor's behavior did not exhibit any sincere effort to control expenses in an honest effort to repay creditors.<sup>105</sup> The debtor had \$143,000 in unsecured debts on credit cards and other bank credit lines.<sup>106</sup> The court dismissed the case as a substantial abuse of Chapter 7 and stated that the housing expenditure was extravagant and "in excess of a reasonable standard of living."<sup>107</sup>

In another line of cases, some courts have refused to confirm a Chapter 13 plan when debtors upgraded their housing very shortly before filing their bankruptcy petitions. In *In re Rice*,<sup>108</sup> the debtors purchased a new home four months before filing their Chapter 13 petition.<sup>109</sup> The purchase

102. *In re Sturgeon*, 51 Bankr. 82, 83 (Bankr. S.D. Ind. 1985). The creditor objected to the expense because the debtor had previously lived rent-free with her father. *Id.* The court stated that "if she would move out, she would have to commit that amount she is presently paying her father for rental expenses." *Id.*

Other examples of rent expenditures held by the courts to be reasonable include: *In re Sutliff*, 79 Bankr. 151, 153 (Bankr. N.D.N.Y. 1987) (\$350 per month for a single debtor); *In re Struggs*, 71 Bankr. 96, 98 (Bankr. E.D. Mich. 1987) (\$280 per month for a single debtor); *In re Peluso*, 72 Bankr. 732, 733 (Bankr. N.D.N.Y. 1987) (\$250 per month for a family of two); *In re Hudson*, 64 Bankr. 73, 74-75 (Bankr. N.D. Ohio 1986) (\$325 per month for a family of five); *In re Tinneberg*, 59 Bankr. 634, 635 (Bankr. E.D.N.Y. 1986) (\$465 per month for a family of two).

103. 886 F.2d 123 (6th Cir. 1989). This was actually a determination of "substantial abuse" in regard to a Chapter 7 petition. *Id.* at 125.

104. *Id.* In connection with the purchase, the debtors reaffirmed a \$19,626 unsecured Mastercard debt with the mortgage lender. *Id.*

105. *Id.* at 127-28 ("At no point in the debtor's history, either before or after filing for chapter 7 relief, has the debtor shown a sincere resolve to repay his obligations and/or to reduce his monthly expenses."). The court was considering whether to dismiss the Chapter 7 case as a substantial abuse under 11 U.S.C. § 707(b) (1988). *Krohn*, 886 F.2d at 125.

106. *Id.*

107. *Id.* at 127. Another court found that a \$989 per month mortgage payment was "well above the amount necessary to provide adequate housing for a family of four." *In re Jones*, 55 Bankr. 464, 467 (Bankr. D. Minn. 1985).

108. 72 Bankr. 311 (D. Del. 1987).

109. *Id.* at 312.

increased their monthly mortgage payment from \$650-\$700 per month to over \$1,100 per month.<sup>110</sup> The debtors' Chapter 13 plan proposed to keep the house and "two relatively new automobiles, while the unsecured creditors got no more than 13 cents on the dollar."<sup>111</sup> The bankruptcy court had found that "[t]he Debtors' plunge into bankruptcy was precipitated by the attempt to enhance their lifestyle by purchasing a new home . . . . Now, Debtors propose a Plan that would permit them to maintain this recently acquired lifestyle at the expense of the unsecured creditors."<sup>112</sup> The district court affirmed the bankruptcy court's denial of plan confirmation because the debtors had an ability to make payments greater than those proposed in their Chapter 13 plan.<sup>113</sup> The court stated that "[a] Plan which allows Debtors to keep the spoils of this purchase, while the unsecured creditors receive only 13 cents on the dollar, is not a Plan that can be confirmed by this Court."<sup>114</sup> Another court dismissed a Chapter 7 case under section 707(b) of the Code because the debtor attempted to upgrade his housing expenditures by moving into a more expensive apartment shortly after filing the Chapter 7 petition. The court held that the higher rent was an attempt by the debtor to inflate expenses to make it appear he did not have any disposable income with which to fund a Chapter 13 plan.<sup>115</sup>

The cases in which the bankruptcy courts have found housing expenditures excessive are the exception to the rule. Absent any obviously extravagant amount or any attempt to upgrade through bankruptcy, the cases indicate that bankruptcy courts approve the debtor's housing expenditures as reasonable and thereby defer to the debtor's judgment as to where to live.

One issue that courts and attorneys should consider when assessing a debtor's housing expenditures is the possible adverse tax consequences of forcing the debtor to sell a home and either rent or purchase a less expensive home. The income tax advantages of deducting mortgage interest are often a consideration when a family chooses the level of mortgage they can afford. If a court required a debtor to sell a home and move into a less expensive home to reduce expenses and increase disposable income, the debtor's disposable income might actually be reduced because of the loss of the

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110. *Id.*

111. *Id.* at 311.

112. *Id.* at 312.

113. *Id.* The District Court noted that this ability to pay would require the debtors to sell their current home and purchase a new one in the price range of their previous home. The court stated that "[t]he alternative is a return to the lifestyle Debtors enjoyed, and seemed able to afford, before their financial turmoil began." *Id.*

114. *Id.* at 313.

115. *In re Ploegert*, 93 Bankr. 641, 643 (Bankr. N.D. Ind. 1988). The debtor's rent increased from \$260 to \$550 per month. *Id.*

income tax deduction, which could offset any reduction in expenses due to the decreased mortgage payment.<sup>116</sup> In addition, the forced sale could cause a loss of equity for the debtor because of the potential for a lower selling price in a distressed sale situation.<sup>117</sup> These considerations led one commentator to conclude that "when considering the reasonableness of a debtor's projected housing costs . . . bankruptcy courts should consider not only the gross reduction in living expenses, but also the potential loss of equity, moving expenses, and noneconomic costs which any move would entail."<sup>118</sup>

One court addressed the income tax consequences of forcing a debtor to sell an expensive home and move to a less expensive home.<sup>119</sup> The debtors had a family of four and a mortgage payment of \$1677 per month on a 3,200 square foot home.<sup>120</sup> The court noted that the debtors had decided to "stretch" their budget and to purchase a large home "as an investment" and that "to make the large mortgage payments required and to maintain their lifestyle, the debtors accumulated large credit card and charge account debts."<sup>121</sup> The debtors maintained that they could sell the home and move into a \$1,000 per month rental home.<sup>122</sup> They argued, however, that the lost income tax deduction would increase their tax liability and, therefore, offset any reduction in living expenses.<sup>123</sup> The court concluded that the debtors' mortgage payment was unreasonable and noted that they should be able to rent a home for a family of four for less than \$1,000 per month.<sup>124</sup> In its discussion of the tax consequences, however, the court did not foreclose the possibility that tax considerations could enter into a determination of whether requiring less expensive housing would be warranted. The court implied that the main factor in considering whether a debtor should sell a residence and

116. The income tax deduction for mortgage interest has the effect of reducing a taxpayer's taxable income, and, consequently, the income tax liability. Thus, the loss of an income tax deduction could increase the debtor's income tax liability. This increased tax liability would reduce the debtor's net income and, thereby, offset any reduction in the debtor's necessary living expenses that resulted from a move to less expensive housing.

117. "If the debtor had to sell a residence in a tight real estate market, he probably would lose a significant amount of equity in the home. Also, the debtor's moving costs could outweigh the savings realized by reduced monthly rental or mortgage payments." Morris, *supra* note 9, at 159 (footnote omitted).

118. *Id.*

119. *In re Kitson*, 65 Bankr. 615 (Bankr. E.D.N.C. 1986).

120. *Id.* at 616-17. The cost of the home was \$180,000 and the principal balance on the mortgage loan was \$170,000. *Id.* at 616.

121. *Id.*

122. *Id.* at 618.

123. *Id.*

124. *Id.* at 621.



move to a less expensive residence is whether the move would reasonably increase the dividend to general unsecured creditors.<sup>125</sup>

A debtor's housing expenditure is one expense category that the courts could use an objective standard to judge reasonableness. Lenders commonly use such a standard for approving residential loans; the loan will not be approved if the monthly payment on the loan exceeds a certain percentage of the borrower's monthly income.<sup>126</sup> Using this same approach, bankruptcy courts could establish a percentage limit to use in analyzing a debtor's monthly housing expenditure. For example, they could use twenty-five percent of net income as the percentage limit.<sup>127</sup> If the debtor's housing expenditure was less than twenty-five percent of his net income, the expenditure would be presumed reasonable. The court would use its discretion for cases in which the expenditure exceeded twenty-five percent of net income, and compelling circumstances existed.

This approach is appealing for several reasons. First, the analysis would be consistent nationwide because it is based on an objective standard. Second, it would be consistent with lender practices. Third, this approach should help compensate for geographical differences in housing costs because it is linked to the debtor's income, and incomes generally fluctuate nationally to reflect differences in costs of living. Finally, because the approach is tied to the debtor's income, it allows the debtor discretion to choose housing commensurate with his or her income level. This approach, however, does present at least one problem. Debtors in the lower income levels are more likely to spend a larger percentage of their income on housing than are debtors in higher income brackets. Lower income debtors may exceed the percentage limitation standard even though they keep very tight control over other expenses, while higher income debtors may meet the percentage limitation standard even though they spend excessively in other areas. In this situation, either the court could use its discretion to account for the lower income discrimination, or the percentage limitation standard could be indexed by income levels to account for the higher percentage expenditure required in the lower income levels.

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125. *Id.*

126. For example, in the Kansas City, Missouri area a common rule of thumb is that the monthly mortgage payment cannot exceed 30% of the borrower's monthly gross income.

127. An analysis of twenty cases, *see supra* notes 97-123, in which the court discussed reasonable housing expenses indicated that the housing expenditure averaged 23.5% of net income. In four of the cases the expenditure exceeded 25% of net income. In one case the expenditure was 46%. The debtor in that case, however, had a net income of \$760 per month. The percentage expenditure for mortgage payments averaged approximately 5% more than that for rent payments. Thus, the 25% of net income percentage limitation would not be inconsistent with past judicial results.

### B. Food: A Fairly Conservative Standard

The bankruptcy court decisions considering what expenditures for food are reasonably necessary have not been consistent. Courts scrutinize the debtor's food budget closely. They consider the ages of any children involved and the size of the family in determining an appropriate food budget. Generally, the courts reject amounts that would appear excessive to almost any reasonable person.<sup>128</sup> One court stated its standard of reasonableness for a family with two children at home: "a low level budget for the Midwest would yield \$293.00 per four week period, a moderate level budget would yield \$368.00, and a liberal level \$433.25."<sup>129</sup>

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128. Budgeted expenditures per month for food which the courts have held to be unreasonable include: *Waite v. Braley*, 110 Bankr. 211, 215 (E.D. Va. 1990) (\$700 per month for a family of four); *In re Reyes*, 106 Bankr. 155, 158 (Bankr. N.D. Ill. 1989) (\$300 per month for a single debtor); *In re Strange*, 85 Bankr. 662, 663 (Bankr. S.D. Ga. 1988) (\$400 per month for a family of two); *In re Stein*, 91 Bankr. 796, 802 (Bankr. S.D. Ohio 1988) (\$780 per month for a family of five); *In re Hudson*, 64 Bankr. 73, 75 (Bankr. N.D. Ohio 1986) (\$600 per month for a family of five); *In re Jones*, 55 Bankr. 464, 467 (Bankr. D. Minn. 1985) (\$515 per month for a family of four); *In re Shands*, 63 Bankr. 121, 123 (Bankr. E.D. Mich. 1985) (\$636 per month for a family of three); *In re Kress*, 57 Bankr. 874, 876 (Bankr. D.N.D. 1985) (\$500 per month for a family of four with monthly income of 6,470).

By way of comparison, budgeted food expenditures held to be reasonable include: *In re Killough*, 900 F.2d 61, 62 (5th Cir. 1990) (\$225 per month for a family of two); *In re LeMaire*, 883 F.2d 1373, 1376 (8th Cir. 1989) (\$175 per month for a single debtor); *In re Gyurci*, 95 Bankr. 639, 641 (Bankr. D. Minn. 1989) (\$350 per month for a family of three); *In re Tefertiller*, 104 Bankr. 513, 514 (Bankr. N.D. Ga. 1989) (\$600 per month for a family of four); *In re Peluso*, 72 Bankr. 732, 733 (Bankr. N.D.N.Y. 1987) (\$320 per month for a family of two); *In re Easley*, 72 Bankr. 948, 949 (Bankr. M.D. Tenn. 1987) (\$200 per month for a single debtor); *In re Struggs*, 71 Bankr. 96, 98 (Bankr. E.D. Mich. 1987) (\$250 per month for a single debtor. However, the debtor did have some responsibilities for a dependent child from a recent divorce); *In re Sutliff*, 79 Bankr. 151, 153 (Bankr. N.D.N.Y. 1987) (\$100 per month for a single debtor); *In re Greer*, 60 Bankr. 547, 549 (Bankr. C.D. Cal. 1986) (\$300 per month for a family of four); *In re Kitson*, 65 Bankr. 615, 617 (Bankr. E.D.N.C. 1986) (\$400 per month for a family of four); *In re Walton*, 69 Bankr. 150, 152 (Bankr. E.D. Mo. 1986) (\$175 per month for a family of four); *In re Tinneberg*, 59 Bankr. 634, 635 (Bankr. E.D.N.Y. 1986) (\$175 per month for a family of two); *In re Schyma*, 52 Bankr. 52, 57 (Bankr. D. Minn. 1985) (\$300 per month for a family of seven).

129. *In re Grant*, 51 Bankr. 385, 395-96 (Bankr. N.D. Ohio 1985) (citation omitted). The debtor had budgeted \$700 per month. The court considered many expenses excessive and dismissed the Chapter 7 petition under the substantial abuse standard of 11 U.S.C. § 707(b) (1988). *Grant*, 51 Bankr. at 395-96.

Food expense is another expense category that the courts could establish an objective standard for reasonableness. The standard should be established on a per person basis rather than as a percentage of net income because food expenses are a necessity that do not fluctuate according to income level. An examination of 23 cases<sup>130</sup> that addressed the issue of food expenditures indicates that the average amount budgeted was \$191 per month per person. The average amount spent per person for plans that the courts confirmed, however, was \$141 while the average for plans the courts refused to confirm was \$210. Based on this analysis, the courts seem to require a budgeted amount somewhere between \$100 and \$150 per person. Thus, the courts could establish a standard of \$150 per month for the debtor plus \$100 per month for each additional dependent living with the debtor. Any amount below this upper limit would be presumed reasonable. The court would use discretion for any amount more than the upper limit in cases with compelling circumstances.

The courts have held that food expenditures were excessive when they included amounts for non-grocery items. For example, the courts are sensitive to excessive expenditures for dining out. In one case, a single debtor budgeted \$433 per month for food.<sup>131</sup> The budget for food and recreation included generous amounts for dining out each week.<sup>132</sup> The court criticized the dining-out expenditure and concluded that the debtor's living expenses were "wildly extravagant and excessive."<sup>133</sup> In another case, the debtor proposed an expenditure of \$480 per month for food.<sup>134</sup> That amount included \$50 per month at the grocery store and \$430 per month for eating out at restaurants.<sup>135</sup> The court criticized the amount as excessive and stated that "the most that the Court can conclude is reasonably necessary . . . is \$300 per month."<sup>136</sup> Some courts have been critical of proposed food expenditures that include excessive amounts for cigarettes. One court criticized a debtor's proposed food expenditures because a \$700 per month budget for food for a family with two children included \$200 per month for cigarettes.<sup>137</sup> Another court refused to confirm a plan that included \$97 per month for cigarettes.<sup>138</sup> The court reasoned that the cigarette expenditures

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130. See *supra* notes 128-29 and *infra* notes 131-39.

131. *In re Ploegert*, 93 Bankr. 641, 643 (Bankr. W.D. Ark. 1988).

132. *Id.*

133. *Id.* See also *Bryant*, 47 Bankr. at 24-25 (the court criticized the debtor for proposing \$100 per month for dining out for a family of four).

134. *In re Bell*, 56 Bankr. 637, 639 (Bankr. E.D. Mich. 1986).

135. *Id.*

136. *Id.* at 642.

137. *Waites v. Braley*, 110 Bankr. 211, 216 (E.D. Va. 1990).

138. *In re Peluso*, 72 Bankr. 732, 733 (Bankr. N.D.N.Y. 1987).

were, in reality, recreation expenditures and that the debtor's plan already included \$100 per month for recreation.<sup>139</sup>

### C. Clothing: Courts Use Their Discretion

Courts have generally concluded that expenditures for purchasing, laundering and dry cleaning clothing are a reasonable expense category. An analysis of the cases, however, shows it is difficult to reach a conclusion as to what level of expenditures per month the courts consider reasonable. Clothing expenditures are directly related to the size of the debtor's family and the debtor's type of employment. For example, a debtor employed in a profession that requires a suit for work attire would have higher clothing expenditures than a debtor employed in a manufacturing position or a position that provided work uniforms.<sup>140</sup> Furthermore, expenditures for new clothing are discretionary and are not as necessary for support as food and housing. The courts should limit a Chapter 13 plan to very few expenditures for new clothing to maximize the dividend to unsecured creditors. This is one expense category where a little belt-tightening by the debtor is not a sacrifice of a basic necessity.

Bankruptcy courts generally do not reject clothing expenditures as excessive unless the expenditures are clearly unreasonable.<sup>141</sup> An analysis

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139. *Id.* at 738.

140. For example, one court criticized a proposed expenditure of \$100 per month for clothing for two debtors who were employed as assembly line workers at a General Motors plant. *In re Shands*, 63 Bankr. 121, 123 (Bankr. E.D. Mich. 1985).

141. For example, one court held that \$416 per month for a single debtor employed as a "parts chaser" for General Motors was excessive. *In re Ploegert*, 93 Bankr. 641, 643 (Bankr. N.D. Ind. 1988). Another court concluded that \$600 per month for a debtor and his wife was excessive. *In re Bryant*, 47 Bankr. 21, 24-25 (Bankr. W.D.N.C. 1984).

Other examples of monthly expenditures for purchasing and cleaning clothing which have been rejected as unreasonable include: *In re Helmick*, 117 Bankr. 187, 190 (Bankr. W.D. Pa. 1990) (\$290 per month for a family of two, neither of whom was employed in a profession requiring the purchase of expensive clothing such as suits); *In re Stein*, 91 Bankr. 796, 803 (Bankr. S.D. Ohio 1988) (\$350 per month for a family of five); *In re Grant*, 51 Bankr. 385, 395 (Bankr. N.D. Ohio 1985) (\$565 per month for a family of four); *In re Bryant*, 47 Bankr. at 24-25 (\$600 per month for a family of four. The amount included \$100 per month for laundry when the family owned a washing machine.).

By way of comparison, amounts expended for purchasing and cleaning clothing which the courts have concluded were reasonable include: *In re Killough*, 900 F.2d 61, 62 (5th Cir. 1990) (\$55 per month for a family of two); *In re LaMaire*, 883 F.2d 1373, 1376 (8th Cir. 1989) (\$20 per month for a single debtor); *In re Gyurci*, 95 Bankr. 641

of twenty cases<sup>142</sup> that discussed the debtor's budgeted expenditures for purchasing and cleaning clothes indicate that the average expenditure as a percentage of net income was six percent, and the average expenditure per family member was \$89 per month. The averages for cases where the plans were not confirmed, however, was seven percent and \$108 per person, while the averages for cases where the plans were confirmed was four percent and \$28 per person. The courts could establish an objective standard such as four percent of net income as a ceiling within which to evaluate budgeted clothing expenditures. Any amount below that percentage would be presumed reasonable. Because of variable factors such as work related needs, however, this category may be one that the courts must use discretion in determining the reasonableness of the amount expended.

#### *D. Transportation: Generally Held Reasonable*

Expenditures for transportation are an expense category universally recognized by the courts as a necessary expense. The determination of a reasonable amount, however, is complicated by the wide variety of transportation available to a debtor. Automobiles are available in price ranges from very inexpensive to very expensive. In addition, a debtor can often sell an expensive automobile and acquire a less expensive automobile without the adverse tax consequences inherent in selling a home, as discussed *supra* in Section II.A. of this Comment. Thus, this expense category is one which primarily depends on the debtor's lifestyle decisions. The challenge for a court is to decide what is a reasonable amount to expend for transportation sources within the myriad of possible transportation available to the debtor. In addition to lifestyle, the debtor's employment may require a more upscale automobile than would be considered reasonably necessary for the average debtor. For example, the debtor may need a newer and more reliable vehicle

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(Bankr. D. Minn. 1989) (\$145 per month for a family of five); *In re Sutliff*, 79 Bankr. 151, 153 (Bankr. N.D.N.Y. 1987) (\$35 per month for a single debtor); *In re Struggs*, 71 Bankr. 96, 98 (Bankr. E.D. Mich. 1987) (\$105 per month for a single debtor); *In re Peluso*, 72 Bankr. at 733 (\$70 per month for a family of two); *In re Easley*, 72 Bankr. 948, 949 (Bankr. M.D. Tenn. 1987) (\$30 per month for a single debtor); *In re Greer*, 60 Bankr. 547, 549 (Bankr. C.D. Cal. 1986) (the court held that \$100 per month for clothes and \$75 per month for laundry and cleaning for a family of four was reasonable); *In re Hudson*, 64 Bankr. 73, 74-75 (Bankr. N.D. Ohio 1986) (\$130 per month for a family of five); *In re Walton*, 69 Bankr. 150, 152 (Bankr. E.D. Mo. 1986) (\$65 per month for a family of four); *In re Tinneberg*, 59 Bankr. 634, 635 (Bankr. E.D.N.Y. 1986) (\$40 per month for a family of two); *In re Jones*, 55 Bankr. 464 (Bankr. D. Minn. 1985) (\$290 per month for a family of five); *In re Schyma*, 52 Bankr. 52, 57 (Bankr. D. Minn. 1985) (\$50 per month for a family of seven).

142. See *supra* notes 140-41.

to travel a great distance to work. Another consideration is that an expenditure for a new vehicle may cost less than extensive repairs on an old vehicle. These and other considerations have made transportation expenditures an expense category that is greatly dependent on the courts' discretion.

The bankruptcy courts allow transportation expenditures that are not patently extravagant or luxurious. The courts generally approve the debtor's current expenditures.<sup>143</sup> An analysis of twenty cases<sup>144</sup> that discussed transportation expenditures indicates that the average expenditure proposed in the Chapter 13 plans was fourteen percent of the debtor's net income. The average percentage of net income for plans not confirmed by the courts, however, was sixteen percent, while it was ten percent for the confirmed plans. On the other hand, the courts reject as excessive transportation expenditures that are obviously extravagant or are an attempt to upgrade during bankruptcy.

A leading case on luxury expenditures for transportation is *In re Rogers*.<sup>145</sup> In *Rogers*, the debtor had a \$440 per month payment on a two-year-old red Corvette and a \$180 per month payment on a two-year-old Cavalier.<sup>146</sup> As part of her proposed Chapter 13 plan, the debtor proposed to sell the Cavalier and pay the secured creditor.<sup>147</sup> The debtor, however, planned to retain the Corvette.<sup>148</sup> She argued that "the Bankruptcy code does not require a debtor to dispose of all of life's little pleasures in order to qualify for Chapter 13 relief."<sup>149</sup> The court stated that "the problem is not the description or even the worth of the asset--it's the size of the debt on it."<sup>150</sup> The court concluded that "it's the *payment*—not the possession of an

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143. Some examples of budgeted transportation expenditures held reasonable by the courts include: *Ploegert*, 93 Bankr. at 643 (\$250 per month payment and \$85 per month for insurance and repairs on a single auto); *In re Kitson*, 65 Bankr. 615, 617 (Bankr. E.D.N.C. 1988) (\$458 per month payment and \$60 per month for insurance for two autos); *Peluso*, 72 Bankr. at 733, (\$250 per month for a five-year-old car); *Greer*, 60 Bankr. at 549 (\$300 per month payment and \$146 per month for auto insurance for a nine-year-old Ford and a three-year-old Toyota); *Jones*, 55 Bankr. at 464 (\$175 per month payment and \$110 per month maintenance and gasoline for a single auto); *Walton*, 69 Bankr. at 152 (\$150 per month for transportation); *Schyma*, 52 Bankr. at 57 (\$543 per month for two used vehicles. One debtor commuted 600+ miles weekly to work).

144. See *supra* note 141 and *infra* notes 144-170.

145. 65 Bankr. 1018 (Bankr. E.D. Mich 1986).

146. *Id.* at 1019-20.

147. *Id.*

148. *Id.* at 1020.

149. *Id.*

150. *Id.* The debtor valued the car at \$14,000 and owed \$17,158.97 on it. *Id.* The court stated that "if the debtor here owned the 'Vette' free and clear, so long as

asset—which is material in an objection under § 1325(b).<sup>151</sup> Finally, the court explained that "the question is how much is a reasonable amount to pay for basic transportation during the period of the Chapter 13 Plan?"<sup>152</sup> The court held that \$440 per month for a two-year-old red Corvette was not reasonable.<sup>153</sup> A significant statement by the court regarding its holding was that car payments for basic transportation should not exceed \$10,000 over a four year period.<sup>154</sup> Thus, it appears that the debtor's budget for transportation expenses must pass the "red Corvette" test.

Another case involving a luxury expenditure on an automobile was *In re Struggs*.<sup>155</sup> In *Struggs*, the debtor proposed to continue \$775 per month payments on a late model Cadillac Fleetwood.<sup>156</sup> The debtor's budget also included \$93 per month for insurance and \$300 per month for gasoline.<sup>157</sup> The court noted that if the debtor used a non-luxury automobile, the expenditures for insurance and fuel would decrease along with the monthly payment.<sup>158</sup> The court held that reasonably necessary expenses for car payment, maintenance, and fuel for basic transportation should not exceed \$300 per month.<sup>159</sup> Thus, the court established an objective standard of \$300 per month for operation of one vehicle.<sup>160</sup> Further, another court

the plan called for paying more than the present value of the non-exempt portion of its value to unsecured creditors, the creditors could not insist that she liquidate the asset and pay the proceeds to them." *Id.* at 1021.

151. *Id.* at 1021. The creditors had argued that the debtor's decision to keep the Corvette "evinces an intent by the debtor to maintain a hot lifestyle at their expense." *Id.* at 1020.

152. *Id.* The court then stated that "this question unavoidably involves the bankruptcy court in difficult value judgments." *Id.* (citations omitted).

153. *Id.*

154. *Id.* at 1021-22. The court stated that the excess over \$10,000 for the Corvette amounted to "luxury" or "recreation" expenses. *Id.*

155. 71 Bankr. 96 (Bankr. E.D. Mich. 1987).

156. *Id.* at 98.

157. *Id.* at 98-99.

158. *Id.* at 99.

159. *Id.* at 98-99. The court cited its holding in *In re Bell*, 56 Bankr. 637, 642 (Bankr. E.D. Mich. 1986).

160. Other examples of budgeted expenditures for transportation held unreasonable by the courts include: *In re Gyurci*, 95 Bankr. 639, 640-641 (D. Minn. 1989) (\$970 per month for all expenses to own and operate five vehicles for a family of five. The children were ages 18, 23 and 25); *In re Stein*, 91 Bankr. 786, 803 (Bankr. S.D. Ohio 1988) (\$465 per month for lease payments and \$235 per month for maintenance and insurance for one automobile); *In re Grant*, 51 Bankr. 385, 395 (\$490 per month lease for a new Nissan and Cutlass Ciera and \$400 per month for maintenance and insurance); *In re Kress*, 57 Bankr. 874, 976 (Bankr. D.N.D. 1985) (\$450 per month for

rejected \$608 per month transportation expenses for a "luxury automobile" as being unreasonable.<sup>161</sup> The court stated that "[g]iven an expected lease payment on a standard car, plus gas and maintenance expenses, the Court concludes that \$300 per month is reasonably necessary for transportation."<sup>162</sup>

These cases in which the courts held transportation expenditures unreasonable illustrate the overriding objective of the courts' lifestyle determination regarding transportation. The courts seek to increase the dividend to general unsecured creditors without drastically altering the debtor's lifestyle. Transportation, however, is one expense category where the courts can increase the dividend with very little sacrifice by the debtor. This is possible because good, reliable, transportation is available at less than extravagant prices.

One court addressed the issue of a debtor attempting to upgrade his transportation through bankruptcy. In *In re Reyes*,<sup>163</sup> just before filing a Chapter 13 petition the debtor purchased a new Chevrolet Blazer at a monthly payment of \$472.<sup>164</sup> The debtor's plan proposed to pay a ten percent dividend to the general unsecured creditors. The court noted that the type of vehicle was not required by the debtor's employment<sup>165</sup> and it concluded that "[t]he Blazer is an 'obvious indulgence' if ever there was one . . ." and that "[t]he Debtor purchased the Blazer simply because he wanted to drive an extravagant four wheel drive vehicle."<sup>166</sup> The court held that the expense was unreasonable because "the sole purpose of filing was to retain the recently purchased Blazer and to make only nominal payments to the unsecured creditors."<sup>167</sup>

In another case with an unpublished opinion, the Bankruptcy Court for the Western District of Missouri denied confirmation of a plan in which the debtor proposed to purchase a vehicle as part of a Chapter 13 plan.<sup>168</sup> The debtor did not own a car prior to filing a Chapter 13 petition.<sup>169</sup> In denying

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a one-year-old Oldsmobile); *In re Bryant*, 47 Bankr. 24-25 (Bankr. W.D.N.C. 1984) (\$731 per month for two Buicks less than one year old).

161. *In re Bell*, 56 Bankr. 637, 642 (Bankr. E.D. Mich. 1986).

162. *Id.*

163. 106 Bankr. 155 (Bankr. N.D. Ill. 1989).

164. *Id.* at 156. The plan also included a \$120 budgeted expenditure for maintenance and gasoline. *Id.*

165. *Id.* at 157 ("The Debtor did not purchase the four wheel drive Blazer to provide a reliable means of transportation to work, for he lived three miles from work and presumably near paved roadways.").

166. *Id.* at 157-58.

167. *Id.* at 156.

168. *In re Johnson*, Case No. 89-41436-W-13 (Bankr. W.D. Mo. 1989).

169. *Id.* The debtor had spent \$78 per month prior to bankruptcy using



confirmation, the court stated that "those living arrangements which the debtor enjoyed prior to filing are the standard form [sic] which the next three to five years should be judged, not the enhanced arrangements to which we all aspire."<sup>170</sup> These decisions indicate that a court will determine if an expensive vehicle is required for employment reasons, and will not allow a debtor to upgrade transportation or purchase a vehicle for the first time through a Chapter 13 plan.

### *E. Recreation: Carefully Scrutinized by the Courts*

The debtor's budgeted recreation expenditures are an expense category that must pass the initial "necessity" threshold. Some bankruptcy courts consider recreation a discretionary and unnecessary expenditure for a Chapter 13 debtor. These courts reason that recreation is an expenditure that can easily be eliminated<sup>171</sup> and that the debtor's general unsecured creditors should not be asked to contribute to the debtor's recreation habits. The majority of courts, however, recognize that the debtor should be allowed some recreational spending during a Chapter 13 plan.<sup>172</sup> For example, one court

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transportation other than an owned vehicle. The debtor's plan proposed a \$150 per month expenditure to purchase a vehicle and \$78 per month for fuel, insurance and maintenance. The plan proposed a 10% dividend to the general unsecured creditors.

170. *Id.* at 2. The court also stated the following:

A debtor's standard in life may frequently be enhanced under a Chapter 13 plan by virtue of the cessation of garnishments, executions and levies, not to mention potential salary increases that creditors are not aware of. However, to deliberately set up a plan that creates a luxury that the debtor has not heretofore enjoyed while paying creditors a minimal sum hardly seems in keeping with the spirit of the law. The Court does not believe that debtors should be abused by their Chapter 13 plan, but neither does the Court believe that creditors should be abused.

*Id.*

In another unpublished opinion, the same court denied discharge of a student loan obligation of a debtor under the "undue hardship" standard of 11 U.S.C. § 523(a)(8) (1988) of the Code in part because the debtor listed a budgeted expense of \$270 per month to purchase an automobile when the debtor did not own an automobile prior to filing a Chapter 7 petition. *In re Hayes*, Case No. 90-20141-C (Bankr. W.D. Mo. 1990). The court stated that "[i]t strikes the Court that she [the debtor] has and can develop employment opportunities without a car and sufficient social development without a car based on her past experience." *Id.* at 2.

171. One commentator categorized expenditures such as this as "discretionary expenses." Corish & Herbert, *supra* note 2, at 70.

172. *In re Edwards*, 50 Bankr. 933 (Bankr. S.D.N.Y. 1985). The court stated that "some recreation is justifiable and beneficial to family harmony and happiness." *Id.* at 940 n.9.

stated that a creditor's objection to a \$12 per month recreation expenditure for newspapers and periodicals was "not only spurious, it is downright heartless."<sup>173</sup> Even these courts, however, scrutinize very carefully the budgeted expenditures for recreation.<sup>174</sup> An analysis of twenty-one cases<sup>175</sup> that discussed budgeted recreation expenditures indicates that the average expenditure proposed in the plans was six percent of the debtor's net income or \$112 per family member. The averages for plans that the courts refused to confirm, however, were eight percent of net income and \$124 per family member compared to five percent and \$46 for plans that were confirmed.

A problem arises, however, as to what is an allowable minimal amount. At a minimum, courts consistently refuse to confirm expenditures for recreational assets such as boats or motor homes which they consider luxury assets. For example, one court refused to confirm a plan that included a \$187 per month payment for a recreational boat.<sup>176</sup> The court referred to the "luxury goods and services" standard in section 523(a)(2)(C) of the Code as one basis for its decision.<sup>177</sup> Under that section, a bankruptcy court may deny discharge of certain consumer debts incurred to purchase "luxury goods or services" that meet certain specific criteria.<sup>178</sup> The court concluded that

173. *In re Tinneberg*, 59 Bankr. 634, 635 (Bankr. E.D.N.Y. 1986) (footnote omitted). The debtor's Chapter 13 plan proposed an 11% dividend for general unsecured creditors which would have been raised to 12% by the elimination of the newspaper expenditure. *Id.*

174. "Although some courts have disallowed recreational expenditures, the determinative factor seems to be the extravagance of the expenditure rather than a feeling that some recreation is not a basic need." Comment, *Religious Debtor's*, *supra* note 29, at 886. One commentator stated that the courts examine a debtor's discretionary expenses "with a close and often jaundiced eye." *Corish & Herbert*, *supra* note 2, at 70.

175. See *supra* notes 170-71 and *infra* notes 176-194.

176. *In re Hedges*, 68 Bankr. 18 (Bankr. E.D. Va. 1986).

177. *Id.* at 20.

178. The section reads in full:

(C) for purposes of subparagraph (A) of this paragraph, consumer debts owed to a single creditor and aggregating more than \$500 for "luxury goods or services" incurred by an individual debtor on or within forty days before the order for relief under this title, or cash advances aggregating more than \$1,000 that are extensions of consumer credit under an open end credit plan obtained by an individual debtor on or within twenty days before the order for relief under this title, are presumed to be nondischargeable; "luxury goods or services" do not include goods or services reasonably acquired for the support or maintenance of the debtor or a dependent of the debtor; an extension of consumer credit under an open end credit plan is to be defined for purposes of this subparagraph as it is defined in the Consumer Credit Protection Act (15 U.S.C. 1601 et seq.). . . .

the boat was a luxury good, and that a luxury good not related to employment was an unnecessary Chapter 13 recreation expenditure.<sup>179</sup> The court stated that "[a] fundamental purpose of the disposable income provision is to prevent large expenditures by debtors for non-essential items which ultimately reduce the sum available to pay holders of unsecured claims."<sup>180</sup> Another court held that a \$598 per month payment to a secured creditor for a motor home was unnecessary and a luxury recreational asset.<sup>181</sup>

The bankruptcy courts generally require a debtor to reduce or eliminate recreation expenditures before they will confirm the debtor's Chapter 13 plan. As noted above, the reductions are amounts that the courts deem to be luxurious or unreasonable. It is difficult to determine what criteria or standard the courts use in this determination because the results reached among the various jurisdictions vary greatly.<sup>182</sup> One general observation from the cases is that the courts evaluate recreation expenditures with reference to the debtor's overall budget and to the amount the debtor proposes to pay to the general unsecured creditors under the plan.<sup>183</sup> A plan proposing a very low or nominal dividend to general unsecured creditors is less likely to have recreation expenditures approved than a plan that proposes a substantial dividend to the unsecured creditors. Also, some courts consider the debtor's

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11 U.S.C. § 523(a)(2)(C) (1988).

179. *Hedges*, 68 Bankr. at 20-21 ("The purpose of § 1325(b) would be ill-served if the Court were to allow the debtor in the instant case to retain possession of purely recreational property not reasonably necessary for maintenance or support of the debtor or his dependents while his general unsecured creditors are to receive over an extended period of time, less than half of the total amount of their claims.").

180. *Id.* at 20.

181. *In re Struggs*, 71 Bankr. 96, 98 (Bankr. E.D. Mich. 1987). The court noted that the extra disposable income generated by not keeping the motor home would allow the debtor to repay general unsecured creditors in full in 16 months. *Id.*

182. One commentator noted the following:

The courts have not been as uniform in their review of expenses for recreation in general. One court held that \$50 per month for a single man was unreasonable. Yet another court described a single woman's \$50 per month expense for recreation as reasonable but went on to deny confirmation of the debtor's plan, holding that a large part of the debtor's sports car payments (her second car) should be allocated to recreation. Yet another court held that \$100 per month for recreation for a family of three was unreasonable and \$50 per month was reasonable (citations omitted).

Butler, *supra* note 10, at 413.

183. "The few courts who have encountered recreation as an expense in a budget pursuant to a Chapter 13 plan have analyzed it by placing the debtor's overall lifestyle and submitted budget into a reasonable and necessary framework." *In re Sutliff*, 79 Bankr. 151, 158 (Bankr. N.D.N.Y. 1987).

marital status, the debtor's geographical area of residence, and the ages of any dependents.<sup>184</sup> One cannot predict, however, if an unmarried debtor is more likely to be allowed more recreation expenses than a married debtor, or if a debtor with older dependents will be allowed more for recreation than a debtor with young dependents. One court implied there may be a percentage ceiling for recreation expenditures.<sup>185</sup> The court stated that it could not confirm a plan "with an entertainment allowance which represents a relatively large chunk of the debtor's net monthly income and half of the proposed monthly payment."<sup>186</sup>

Some proposed recreation expenditures raise a red flag and are generally disfavored. For example, budgeted expenditures for cable television,<sup>187</sup> dining out,<sup>188</sup> country club dues<sup>189</sup> and health club memberships<sup>190</sup> have

184. "The amount of recreation in each Chapter 13 budget is a fact question that must be determined in the individual context of each debtor and his dependents." *Id.*

185. The court rejected the debtor's recreation budget as unreasonable and noted that the "budget allocates more than six and one-half percent of his net monthly income to recreation." *Id.*

186. *Id.* at 159.

187. *Waites v. Braley*, 110 Bankr. 211, 215 (E.D. Va. 1990) (the debtor budgeted \$240 per month for recreation for a family of four and the amount included \$36 for cable television where the Trustee had argued that the cable television was unnecessary); *See also In re Helmick*, 117 Bankr. 187, 190 (Bankr. W.D. Pa. 1990) (court critical of unspecified expenditure for cable television); *In re Ploegert*, 93 Bankr. 641, 643 (Bankr. N.D. Ind. 1988) (court regarded as excessive an \$840 per month budget for recreation for a single debtor that included \$35 per month for cable television); *In re Grant*, 51 Bankr. 385, 395 (Bankr. N.D. Ohio 1985) (court concluded a \$475 per month budget for recreation for a family of four which included \$25 per month for cable television was excessive); *In re Bryant*, 47 Bankr. 21, 26 (Bankr. W.D.N.C. 1984) (\$65 per month for cable television regarded as not reasonably necessary).

*But cf. In re Killough*, 900 F.2d 61, 62 (5th Cir. 1990) (the court affirmed a bankruptcy court's determination that \$27 per month for cable television was a reasonable recreation expenditure).

188. *Waites*, 110 Bankr. at 216 (court criticized a debtor's budget of \$204 for recreation expenses for a family of four in part because it provided for eating out twice a month); *Ploegert*, 93 Bankr. at 643 (court considered an \$840 per month recreation budget which included "dining out on a weekly basis" for a single debtor to be excessive); *Bryant*, 47 Bankr. at 26 (\$100 per month for eating out for a family of four considered excessive).

189. *In re Chrzanowski*, 70 Bankr. 447, 450 (Bankr. D. Del. 1987).

190. *In re Kitson*, 65 Bankr. 615, 622 (court considered unnecessary a proposed expenditure of \$48 per month for a health club membership as part of a budget of \$275 per month for recreation for a family of four). *But cf. In re Schyma*, 68 Bankr. 52, 57 (Bankr. D. Minn. 1985) (the court allowed a \$25 per month expenditure for club dues for a family of seven).

all been criticized by the courts as being either unnecessary or excessive expenditures for a Chapter 13 debtor. Apart from these expenditures, however, the courts allow at least some recreation expenditures in a Chapter 13 plan and will confirm plans with modest recreation expenditures.<sup>191</sup>

Bankruptcy courts often discuss proposed expenditures for newspapers and periodicals as a separate expense category, but they could be considered a part of the debtor's recreation expenses.<sup>192</sup> Generally, the courts allow some expenditure for newspapers or periodicals.<sup>193</sup> The courts usually, however, require the debtor to specify which newspapers and periodicals are being considered and to propose exact amounts for subscriptions.<sup>194</sup>

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191. Examples of budgeted recreation expenditures that have been allowed as reasonable by the courts include: *In re Tefertiller*, 104 Bankr. 513, 515 (Bankr. N.D. Ga. 1989) (\$200 per month for a family of four); *In re Stein*, 91 Bankr. 786, 798 (Bankr. S.D. Ohio 1988) (\$50 per month for a family of five); *In re Struggs*, 71 Bankr. 96, 98 (Bankr. E.D. Mich. 1987) (\$50 per month for a single debtor); *In re Peluso*, 72 Bankr. 732, 733 (Bankr. N.D.N.Y. 1987) (\$100 per month for a family of two); *In re Rogers*, 65 Bankr. 1018, 1019 (Bankr. E.D. Mich. 1986) (\$40 per month for a single debtor); *In re Walton*, 69 Bankr. 150, 152 (Bankr. E.D. Mo. 1986) (\$40 per month for a family of four); *In re Schyma*, 68 Bankr. 52, 57 (Bankr. D. Minn. 1985) (\$30 per month for a family of seven).

For purposes of comparison, budgeted amounts for recreation expenditures which have been criticized by the courts as unreasonable include: *In re Helmick*, 117 Bankr. 187, 190 (W.D. Pa. 1990) (\$100 per month for a family of two); *In re Reyes*, 106 Bankr. 155, 158 (Bankr. N.D. Ill. 1989) (\$120 per month for a single debtor); *In re Sutliff*, 79 Bankr. 151, 156-57 (Bankr. N.D.N.Y. 1987) (\$50 per month for a single debtor); *In re Davis*, 68 Bankr. 205, 215-16 (Bankr. S.D. Ohio 1986) (the court stated that it was arguable that an expenditure of \$30 per month for a family of four was not reasonably necessary); *In re Kelly*, 57 Bankr. 536, 538 (Bankr. D. Ariz. 1986) (\$500 per month); *In re Shands*, 63 Bankr. 121, 123 (Bankr. E.D. Mich. 1985) (\$120 per month for a family of three); *In re Kress*, 57 Bankr. 874, 876 (Bankr. D.N.D. 1985) (\$200 per month for a family of four when monthly income was \$7,500).

192. "A reasonable amount for a local newspaper is also allowable as a basic need." Comment, *Religious Debtor's*, *supra* note 29, at 886 (citations omitted).

193. "No humane standard would prohibit debtors in bankruptcy from buying a newspaper." *In re Tinneberg*, 59 Bankr. 634, 635 (Bankr. E.D.N.Y. 1986).

194. Examples of amounts for newspapers and periodicals held by the courts to be unreasonable expenditures for a Chapter 13 debtor include: *Waites v. Braley*, 110 Bankr. 211, 215 (E.D. Va. 1990) (\$90 per month for a family of four); *In re Ploegert*, 93 Bankr. 641, 643 (Bankr. N.D. Ind. 1988) (\$65 per month for a single debtor); *In re Hudson*, 64 Bankr. 73, 75 (Bankr. N.D. Ohio 1986) (\$30 per month for a family of five. The court stated in footnote 1 that "a subscription to the local newspaper is \$15 per calendar quarter, or approximately \$4.60 per month. The remaining \$23.40 of the \$30.00 per month listed by the Debtors is unaccounted for."); *In re Kitson*, 65 Bankr. 615, 622 (Bankr. E.D.N.C. 1986) (\$24 per month for a family of four); *In re Davis*,

The courts should be able to establish an objective standard for determining reasonable recreation expenditures. For example, a standard of three percent of net income could be used as a ceiling for recreation expenditures. This amount would allow at least a modest amount for every debtor and provide a presumption of reasonableness for any amount below three percent. The courts could use their discretion in cases with compelling circumstances.

#### *F. Education: Absence of Case Law*

A debtor's proposed Chapter 13 expenditures for private or parochial school education present a dilemma for the bankruptcy courts. The critical issue is whether a debtor should be able to budget for expensive private or parochial school education when free public education is available. Expressed another way, should general unsecured creditors be forced to subsidize an expensive education for a debtor's dependents since funds that otherwise would be paid to them are being used for education? This expense category presents such a complex issue because it involves questions of public policy and individual social values. The public policy issues relate to the quality of public education in a particular area. The complexity is increased by the potential impact on the debtor's dependents and the debtor's religious convictions. Regarding the debtor's dependents, the question is whether the debtor's financial woes should adversely affect the quality of a dependent's education? In the parochial school context, the issue is one relating to religious beliefs. If the debtor believes it is a religious duty to send his children to a parochial school, should the court be able to limit or deny his or her ability to do so? Creditors argue that private education is not a right of citizenship. Therefore, it is not permissible to force them to contribute to private or parochial education when the debtor's income, apart from Chapter 13 assistance, is not sufficient to provide for it.

Education is an expense category that some bankruptcy courts have concluded is not a reasonably necessary expenditure for a Chapter 13 debtor. Those courts hold that private or parochial education expenditures are never reasonably necessary for support or maintenance of a debtor or his dependents. Few courts, however, have addressed the issue of reasonably necessary

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68 Bankr. 205, 215-16 (Bankr. S.D. Ohio 1986) (\$50 per month for a family of four where the court stated that it is arguable that the expense is not reasonably necessary).

Examples of expenditures that the courts have held to be reasonable include: *In re Jones*, 55 Bankr. 464 (Bankr. D. Minn. 1989) (\$30 per month for a family of five); *Struggs*, 71 Bankr. at 98 (\$12 per month for a single debtor); *Walton*, 69 Bankr. at 152 (\$5 per month for a family of four); *In re Bryant*, 47 Bankr. 21, 24 (Bankr. W.D.N.C. 1984) (\$25 per month for a family of four).

educational expenses. One court held that \$500 per month for tuition to a private college and \$500 per month for tuition to a parochial high school were not necessary for support or maintenance of the debtor's dependents.<sup>195</sup> The court stated that "an expensive private school education is not a basic need of the Debtor's dependents, particularly in view of the high quality public education available in this country at both the collegiate and secondary school levels."<sup>196</sup> In spite of this language, the court proceeded to reduce the Chapter 13 plan's total allowed expenses by only \$377.54 per month.<sup>197</sup> Another court held that \$395 for an "exclusive private high school" may not be reasonably necessary.<sup>198</sup>

Not all courts, however, have disallowed proposed Chapter 13 educational expenditures. For example, one court held that \$160 per month for college tuition and \$69 per month for a special school for a disabled daughter were reasonably necessary.<sup>199</sup> The court never stated whether the son attended a public or private school, but it is likely that his \$160 per month college tuition was for a public college or university. Also, the \$69 per month tuition for a special school could be distinguished from other private school expenditures because it was required as a result of the dependent's disability. Thus, it is possible that courts could consider public school tuition and *required* private school tuition as necessary expenses. The rationale would be that it is not reasonable to deny the debtor the opportunity to assist dependents with educational expenses so long as the expenditures are not for discretionary private school expenses. At least one court, however, has held that \$100 per month for a parochial school was reasonably necessary.<sup>200</sup> The court reasoned that the parochial school tuition was not a luxury expenditure and the debtor "[o]btained no tangible benefit or increased standard of living because of the money expended."<sup>201</sup>

Due to the lack of cases discussing this expense category, it is almost impossible to reach a conclusion regarding allowable education expenditures. Probably, public school tuition and required private school tuition have a greater chance of being allowed by the courts in a Chapter 13 plan than private or parochial school tuition expended for purely personal reasons. There are arguable policy reasons for denying private school tuition because

195. *Jones*, 55 Bankr. at 467.

196. *Id.*

197. *Id.*

198. *In re Gyurci*, 95 Bankr. 639, 643 (Bankr. D. Minn. 1989).

199. *In re Hudson*, 64 Bankr. 73, 75 (Bankr. N.D. Ohio 1986).

200. *In re Navarro*, 83 Bankr. 348, 356 (Bankr. E.D. Pa. 1988) ("I am not prepared to conclude that tithing and religious education are *per se* unreasonable choices for the maintenance and support of a chapter 13 debtor's family.").

201. *Id.*

of available public education. Also, the reduced cost for public education would leave more of the debtor's funds available to repay general unsecured creditors. The parochial school issue is more complex because of the religious convictions of the debtor. The problems attendant with denying exercise of religious convictions during a Chapter 13 plan are discussed *infra* in Section II. H. of this Comment in connection with a discussion of the religious contribution expense category.

### G. Contingency Fund: Minimal Amounts Allowed

Most debtors include in their proposed Chapter 13 plan an amount commonly referred to as a "contingency fund." The idea is that a debtor should have an amount budgeted for unspecified expenditures that may arise during the course of the plan. The expenditures may be for unanticipated emergencies or for items that do not fit other expense categories. As a result, the contingency fund can be thought of as a "miscellaneous" expense category. The fund is the expense category most scrutinized by the courts since it represents a non-specified fund<sup>202</sup> and most courts question either the necessity for the fund or the reasonableness of the amount proposed. Creditors argue that this contingency amount should not be included in the debtor's budget as a reasonably necessary expense. The problem, however, is that "personal expenses do not arrive in monthly lumps."<sup>203</sup> Without at least some cushion for unexpected expenses, the debtor may not be able to complete the plan as proposed.

Some courts hold that a contingency fund is not a reasonably necessary expense in a Chapter 13 plan because section 1329 of the Code allows modification of a plan by either a debtor or a creditor after confirmation if the debtor's circumstances change. Other courts have held, however, that using section 1329 to modify a plan each time an unforeseen expense arises would be a waste of judicial time and resources. For example, one court stated that to reject a contingency fund and rely on modification would "cause additional time and expense to the debtor, his counsel and the trustee in constantly amending the plan to reflect the changes to the debtor's regular income and expenses, not to mention burdening the court's calendar."<sup>204</sup> One commentator suggested that not allowing the Chapter 13 debtor a contingency fund for emergencies would be a violation of the feasibility test of section 1325(a)(6) because it is unlikely that the debtor would be able to complete the plan

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202. One commentator referred to the contingency fund as an "area of controversy" in the reasonably-necessary-expenses determination for the disposable income test. Butler, *supra* note 10, at 413.

203. Gross, *supra* note 24, at 69.

204. *In re Belt*, 106 Bankr. 553, 562 (Bankr. N.D. Ind. 1989).



without it.<sup>205</sup> Another commentator has suggested that "to the extent that the court is concerned about the retention of excessive contingency reserves, it could require the debtor to account for any unspent and uncommitted reserves at the end of the plan, and to make a final dividend to creditors of whatever excess remained."<sup>206</sup>

Bankruptcy courts are evenly split as to whether a contingency fund is a reasonably necessary expense. The courts that have addressed the issue recognize that "the Code requires a meaningful and realistic budget accompanied by devotion of most of the debtor's surplus income to repay creditors."<sup>207</sup> Despite the desire to maximize the dividend of general unsecured creditors, some courts conclude that an amount budgeted for contingencies is a reasonable expense category for a Chapter 13 plan.<sup>208</sup> For example, in *In re Otero*,<sup>209</sup> the court held that \$117 per month for contingencies was an acceptable amount.<sup>210</sup> The court stated that "a cushion of money is necessary in Chapter 13 budgeting to guard against life's unexpectancies. It is not in the public interest to squeeze the last dollar from Chapter 13 debtors to fund a Chapter 13 plan."<sup>211</sup> In another case, a California court allowed as reasonable a proposed contingency fund of \$75 per month for a family of four.<sup>212</sup> The court reasoned that the contingency reserve was necessary

205. Butler, *supra* note 10, at 413. See also *In re Coffman*, 90 Bankr. 878, 884 (Bankr. W.D. Tenn. 1988) ("there is ample authority for the proposition that in order to meet the feasibility requirements of the Bankruptcy Code, a plan should provide for a 'cushion' of money 'to guard against life's expectancies [sic]"); Collier, *supra* note 19, at para. 1325.08 (citations omitted) ("Many courts, in considering whether a plan is feasible under section 1325(a)(6) of the Code, have noted that a realistic budget must include some margin for such expenses.") (citations omitted).

206. Corish & Herbert, *supra* note 2, at 69.

207. *In re Belt*, 106 Bankr. 553, 562 (Bankr. N.D. Ind. 1989).

208. In a reference to Section 1325(b) of the Code, one court stated that "a reasonable reserve or contingency fund does not violate that section." *Id.* See also *In re Fries*, 68 Bankr. 679, 683 n.7 (Bankr. E.D. Pa. 1986).

One commentator concluded that "the majority of cases, however, have allowed the debtor to retain a monthly surplus of various amounts, apparently holding that such a surplus is a reasonable and necessary expense and as such is not part of the debtor's projected disposable income". Butler, *supra* note 10, at 413 (citations omitted). See also Collier, *supra* note 19, at para. 1325.08 ("It is also clear from the legislative history that the amount necessary for support of the debtor and the debtor's dependents must include a 'cushion' for unexpected expenses.").

209. 48 Bankr. 704 (Bankr. E.D. Va. 1985).

210. *Id.* at 708.

211. *Id.*

212. *In re Greer*, 60 Bankr. 547, 552-53 (Bankr. C.D. Cal. 1986). See also *Fries*, 68 Bankr. at 683 n.7 (\$92.16 per month for a family of five).

because "while improvident spending doubtless accounts for a certain portion of post-petition defaults, it appears that most of the relief from stay litigation results from debtors' simple inability to live within their proposed budgets."<sup>213</sup>

On the other hand, some courts take the position that a contingency reserve is not a reasonably necessary expense and will not allow any amount for it. For example, one court refused to allow a debtor to retain \$35 per month for contingencies.<sup>214</sup> The debtor's plan proposed to pay unsecured creditors approximately twenty percent and proposed to commit \$450 out of \$485 of disposable income.<sup>215</sup> The court interpreted "all" in section 1325(b) to mean that the debtor's entire income net of reasonable expenses must go toward the plan.<sup>216</sup> Another court held that \$40 per month for contingencies for a single debtor was not reasonably necessary.<sup>217</sup>

Even courts that allow the contingency fund will carefully evaluate if the proposed amount of the fund is reasonable.<sup>218</sup> For example, one court stated that \$376 per month for contingencies for a family of four was excessive.<sup>219</sup> The court did not conclude that the budgeted contingency category was unnecessary. Rather, the court criticized the amount as being excessive. In *In re Marshall*,<sup>220</sup> the court implied that a debtor would need to prove the necessity of a contingency fund to include it in the Chapter 13 plan. The debtor proposed to include \$469 per month in his Chapter 13 plan as a "safety cushion" against "fluctuation" of his income.<sup>221</sup> This amount represented thirty-three percent of his disposable income and fourteen percent of his net income.<sup>222</sup> The court stated that it must assume the proposed income will be available "unless the Debtors can make a firm showing that a cushion for

213. *Greer*, 60 Bankr. at 553. The court noted that "debtors in general have been cutting their budgets too thinly to be able to meet their post-petition obligations, including plan payments." *Id.* Also, the court stated that the feasibility test of section 1325(a)(6) would mandate a contingency fund to make sure the debtor could make all payments due under the plan. *Id.*

214. *In re Krull*, 54 Bankr. 375, 377 (Bankr. D. Colo. 1985).

215. *Id.*

216. *Id.* Thus, the court was implying that disposable income did not include a contingency fund for unexpected future expenses.

217. *In re Reyes*, 106 Bankr. 155, 158 (Bankr. N.D. Ill. 1989).

218. "Even if a surplus is allowed, the amount of the surplus is subject to judicial review for reasonableness just like any other expense." *Butler*, *supra* note 10, at 413-14.

219. *In re Kitson*, 65 Bankr. 615, 621 (Bankr. E.D.N.C. 1986). It should be noted, however, that the debtor had also budgeted \$433 for miscellaneous expenses.

220. 111 Bankr. 325 (Bankr. D. Mont. 1990).

221. *Id.* at 327.

222. *Id.*

unexpected necessities is reasonably probable."<sup>223</sup> Thus, the court inferred that a contingency fund can be proposed to cover reasonably probable fluctuations in income, but the court stated that \$469 per month was "patently more than a safety cushion."<sup>224</sup>

Bankruptcy courts sometimes discuss whether a debtor should be allowed to maintain a savings or pension plan or deduction during a Chapter 13 plan. These discussions relate to the concept of a contingency fund because the savings plans can serve the same function as a contingency fund. One commentator stated that "the real issue is whether the money saved is likely to be needed by the debtor during the three year period or not. Obviously, a debtor should not be allowed to save for retirement, or even a mardi gras ending to his penitential three years."<sup>225</sup> One court distinguished between mandatory and voluntary savings accounts.<sup>226</sup> The court noted that a \$30.40 per month payroll deduction for a savings account was "compulsory and a condition for [the debtor's] continued employment."<sup>227</sup> Therefore, the court concluded that "this compulsory monthly payroll deduction is not 'disposable income' because it is akin to an expense necessarily expended if [the debtor] is going to continue to be engaged in her normal business venture of being a teacher."<sup>228</sup>

The few courts that have discussed savings plans have rejected them as an unnecessary expenditure in a Chapter 13 plan.<sup>229</sup> For example, in *In re Festner*,<sup>230</sup> the court held that \$25 per month for voluntary retirement benefits and \$22 per month for a stock savings plan were not reasonably necessary for the debtor's or his dependent's support or maintenance.<sup>231</sup> The court stated that "[a]dditional pension plans and stock purchases may be a wise investment which enhance an individual's financial security, but the

223. *Id.*

224. *Id.*

225. Corish & Herbert, *supra* note 2, at 69.

226. *In re Colon Vazquez*, 111 Bankr. 19 (Bankr. D.P.R. 1990).

227. *Id.* at 20.

228. *Id.* The court concluded that "the deduction fulfills a public policy enunciated by the Legislature of the Commonwealth of Puerto Rico which this Bankruptcy Court will respect and uphold." *Id.*

229. One commentator stated that "several courts have determined that saving for the future is not a present basic need." Comment, *Religious Debtor's*, *supra* note 29, at 885 (citations omitted).

230. 54 Bankr. 532 (Bankr. E.D.N.C. 1985).

231. *Id.* at 533. The plan also included an \$85 per month payment on a loan secured by stock owned by the debtor. *Id.* The court concluded that the payout to unsecured creditors would increase from 42% to 82% if all three payments were added to disposable income.

debtor is not entitled to acquire them at the expense of unpaid creditors."<sup>232</sup> Another court held that a \$12.50 per week deduction for a debtor's savings account was not a reasonably necessary expense.<sup>233</sup> Further, in *In re Bell*<sup>234</sup> the court held that a voluntary annuity contribution of \$820 per month was not a reasonably necessary expenditure.<sup>235</sup> The court stated that "[t]he debtor is apparently saving for his future at the expense of his present creditors; this is simply not reasonably necessary for his support and cannot be condoned."<sup>236</sup> These cases imply that it is important how a debtor characterizes a proposed amount for emergencies in his Chapter 13 plan. A proposed category for contingency fund may have a better chance of being allowed than a proposal to maintain a savings account deduction.

#### *H. Charitable & Religious Giving: A Split Among the Courts*

A complex issue facing bankruptcy courts is whether they can refuse to confirm a plan in which a debtor proposes to contribute monthly to a chosen religious organization.<sup>237</sup> The issue generally arises in the context of "tithing"<sup>238</sup> to a religious organization.<sup>239</sup> One concern is if it would be

232. *Id.*

233. *In re Red*, 60 Bankr. 113, 116 (Bankr. E.D. Tenn. 1986). It is significant to note that 94% of the debtor's unsecured debt was a personal injury judgment from an auto accident and the debtor was proposing to pay only 14% on his unsecured debts. *Id.* at 114.

234. 56 Bankr. 637 (Bankr. E.D. Mich. 1986).

235. *Id.* at 642. *See also In re Chrzanowski*, 70 Bankr. 447, 448 (Bankr. D. Del. 1987) (the court criticized a \$202.75 proposed monthly expenditure which included an amount for a voluntary IRA deduction).

236. *Id.*

237. One court stated the following:

By whatever name or rite, man has and will seek some entity or institution that answers the unanswerable questions and assuages the unassuageable doubts and concerns of our human existence. But that is each person's free choice; to seek or not, to believe or not; to contribute or not; and who or what is right is not for this Court or any other branch of the state or federal government to decide. This Court may not and must not say what if any portion of debtor's income shall go to support his personal religious beliefs, but this Court may determine what constitutes those items reasonably necessary 'to be expended-(A) for the maintenance or support of a debtor or a dependent.'

*In re Reynolds*, 83 Bankr. 684, 685 (Bankr. W.D. Mo. 1988).

238. One commentator defined religious tithing as "the giving of a tenth of the annual produce or other income for the support of a particular religious ministry." Comment, *Resolving the Conflict Between Chapter 13 of the Bankruptcy Code and the*

a constitutional violation to deny a debtor the opportunity to contribute to a religious organization under a Chapter 13 plan. The constitutional arguments are based on the Free Exercise and Establishment Clauses of the First Amendment of the United States Constitution.<sup>240</sup> The debtors argue that if the court refuses to allow an expenditure for religious giving in a Chapter 13 plan, then the court has interfered with the debtor's right to the free exercise of religion.<sup>241</sup> Conversely, the creditors argue that if the court allows a debtor to contribute to a religious organization as a reasonably necessary expenditure under a Chapter 13 plan, then the court is forcing the general unsecured creditors to contribute to the debtor's religious organization, thereby violating the Establishment Clause.<sup>242</sup> Most bankruptcy courts that have addressed the issue of proposed expenditures for tithing have concluded there is no constitutional issue involved.<sup>243</sup> Instead, they maintain that the determination of whether religious giving under a Chapter 13 plan is a reasonably necessary expense is no different from the determination for any other expenditure category.

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*Free Exercise Clause—In Re Green: A Step in the Wrong Direction*, 57 MISS. L.J. 163, 164 n.8 (1987) (quoting Horner, *The Christian and The Tithe*, RESOURCE UNLIMITED 176, 178 (W. Hendrick's ed. 1972)).

239. For a thorough discussion of the constitutional and other issues related to giving to a religious organization as a part of a Chapter 13 plan, see Comment, *supra* note 238, at 164; Comment, *Religious Debtor's*, *supra* note 29.

240. The First Amendment of the United States Constitution reads in relevant part: "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof." U.S. CONST. amend. I.

241. "The debtors argue that their right to tithe is protected by the free exercise clause of the First Amendment and that forcing them to choose between tithing and proposing a confirmable bankruptcy plan by application of the disposable income test would deprive them of constitutionally protected substantive rights." *In re Navarro*, 83 Bankr. 348, 351 (Bankr. E.D. Pa. 1988).

A few courts have agreed that the debtor's right to tithe during the pendency of a Chapter 13 plan is protected by the Establishment Clause. See *In re Green*, 103 Bankr. 852 (Bankr. W.D. Mich. 1988).

242. "[T]he creditor implicitly argues that by allowing the debtor to contribute funds to a church which could otherwise be used to pay unsecured creditors, the court is indirectly compelling the creditor to support religious endeavors in violation of the establishment clause and right to freedom of association found in the First Amendment." *Navarro*, 83 Bankr. at 352. See also *In re Tucker*, 102 Bankr. 219, 220 (Bankr. D.N.M. 1989) ("By allowing a chapter 13 debtor to deduct contributions to any organization, the Court necessarily is forcing the debtor's creditors to contribute to the debtor's church or favorite charity. Congress could have intended no such result.").

243. For example, one court stated that it could "either confirm or refuse to confirm the debtor's plan without violating the constitution." *Navarro*, 83 Bankr. at 354.

Two courts have reasoned that some tithing should be allowed as a reasonable expenditure in a Chapter 13 plan because Official Form 10, item 4(b)(15), authorized by Bankruptcy Rule 9009, provides a space to list "religious and other charitable contributions" in the debtor's budget.<sup>244</sup> The Official Forms were not approved by Congress nor by the Rules Committee, however, and, therefore do not provide any indication of legislative intent.<sup>245</sup>

A majority of the courts that have considered the issue hold that charitable or religious giving is not a reasonably necessary expense for the support of the debtor or a dependent of the debtor in a Chapter 13 plan.<sup>246</sup> One commentator stated that "if charity begins at home, it ends with bankruptcy."<sup>247</sup> In *In re Sturgeon*,<sup>248</sup> the court held that tithing of \$140 per month was not a necessary expense.<sup>249</sup> Another court held that giving \$103 per month to the church was not reasonably necessary.<sup>250</sup> Perhaps the most extreme example of this position on charitable giving is the court that refused to confirm a plan that proposed a \$7 per month payroll deduction for the United Way.<sup>251</sup>

244. *In re Curry*, 77 Bankr. 969, 970 (Bankr. S.D. Fla. 1987). See also *Navarro*, 83 Bankr. at 356.

245. *Curry*, 77 Bankr. at 970.

246. See *In re Reynolds*, 83 Bankr. 684, 685 (Bankr. W.D. Mo. 1988). One commentator stated that "charitable contributions of even very modest amounts have been forbidden." Corish & Herbert, *supra* note 2, at 74 (citations omitted).

247. Corish & Herbert, *supra* note 2, at 74.

248. 51 Bankr. 82 (Bankr. S.D. Ind. 1985).

249. *Id.* at 83.

250. *In re Curry*, 77 Bankr. 969, 969-70 (Bankr. S.D. Fla. 1989). In that case, the debtor proposed a \$125 per month payment to his Chapter 13 plan which would have amounted to a 26% dividend for the unsecured creditors. *Id.* at 969. The court noted that the contribution was "voluntary" and stated that to allow the expense would "permit the debtor to require that *his creditors* contribute to his chosen charity." *Id.* at 970 (court's emphasis).

251. *In re Red*, 60 Bankr. 113, 116 (Bankr. E.D. Tenn. 1986). See also *In re Gyurci*, 95 Bankr. 639, 643 (Bankr. D. Minn. 1989) (the court stated that the debtor could tighten his belt by eliminating a \$100 per month contribution to his church); *In re Tucker*, 102 Bankr. 219, 220 (Bankr. D.N.M. 1989) (the court held that a tithe of \$100 per month was not a reasonably necessary expense for a chapter 13 plan); *In re Davis*, 68 Bankr. 205, 215-216 (Bankr. S.D. Ohio 1988) (the court stated that it is arguable that a church contribution of \$46 per month is not a reasonably necessary expense); *In re Hudson*, 64 Bankr. 73, 75 (Bankr. N.D. Ohio 1986) ("this Court does not favor, during the course of its Chapter 13 cases, the contribution of funds to non-profit institutions for the main reason that these contributions are not included in the provisions of Section 1325, particularly Section 1325(b)(1) and (2)."). *Id.* at 75 n. 1.

A few bankruptcy courts have held, however, that a small amount of giving under a Chapter 13 plan is a reasonably necessary expenditure. For example, one court stated that "some level of religious or charitable contribution and some expenditure on religious education may be consistent with expenditures reasonably necessary for maintenance and support of chapter 13 debtors."<sup>252</sup> In the Western District of Missouri, Judge Koger held that "certainly some nominal amount will be permissible, but that amount will need to be below 3% of gross income unless very unusual circumstances are present."<sup>253</sup> Another court held that \$17 per month for a family of four was a reasonably necessary expenditure.<sup>254</sup> These courts treat religious or charitable giving the same as any other necessary expense category. They presume that tithing or charitable giving is not a luxury expense that increases the debtor's standard of living, but rather is similar to any other expense considered in the disposable income analysis.<sup>255</sup>

Some bankruptcy courts make a distinction between required giving and voluntary giving.<sup>256</sup> One court concluded that the critical factors in analyzing proposed tithing are whether the tithe is mandatory and whether it serves a bona fide religious purpose.<sup>257</sup> The court stated:

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252. *In re Navarro*, 83 Bankr. 348, 356 (Bankr. E.D. Pa. 1988).

253. *In re Reynolds*, 83 Bankr. 684, 685 (Bankr. W.D. Mo. 1988). The court stated that "this Court chooses to establish no hard and fast rule as to what amount or percentage of charitable contribution it will construe as 'reasonably necessary.' That will depend on the circumstances of each case." *Id.* However, the court then held that contributions should not exceed 3% of gross income except in very unusual circumstances. *Id.*

254. *In re Grant*, 51 Bankr. 385, 395 (Bankr. N.D. Ohio 1985).

255. *Navarro*, 83 Bankr. at 356. The court concluded that "religious contributions and parochial school education are not expenses for luxury goods or services. The debtors obtain no tangible benefit or increased standard of living because of the money expended." *Id.*

256. *In re Sturgeon*, 51 Bankr. 82, 83 (Bankr. S.D. Ind. 1985) ("the Court does not believe that there is any church law requiring this donation; it is more a matter of conscience.") Thus, the court held open the possibility that tithing to the church may be a reasonably necessary expense if the particular denomination "required" it. In the case before it, however, the objecting creditor was the estate of a driver killed by the debtor's drunk driving, and the court stated that "under the circumstances presented here it would be more just and more noble a gesture to offer the \$140.00 per month to the Estate of Christopher Helmsing." *Id.* at 83-84. Thus, the holding in that case may be specific to the facts of the case.

257. *In re Bien*, 95 Bankr. 281, 282 (Bankr. D. Conn. 1989). The court stated that:

An expense for a religious tithe must be treated differently. Court scrutiny of such expense should include a determination of whether the proposed expense fulfills a bona fide personal commitment intended to serve or

The church tithe is a condition precedent to full participation in the debtor's religion, and the proposal to incur that expense unquestionably serves a bona fide religious and spiritual purpose . . . . Since the amount is an integral part of the religion rather than a discretionary donation, it is, as noted, beyond the purview of this court's inquiry.<sup>258</sup>

Another court stated that "in the context of a sincerely held belief in a denomination that mandates a tithe, I cannot hold that contribution of a tithe is excessive."<sup>259</sup> It seems, however, that if a court seeks to avoid a discretionary decision of whether a tithe is reasonably necessary by holding that it is reasonable if mandatory, then the court will nevertheless be caught up in a fact intensive discretionary determination of whether a particular tithe is voluntary or mandatory.

Some bankruptcy courts consider the size of the Chapter 13 plan's dividend to general unsecured creditors. In *In re Miles*,<sup>260</sup> the court stated that the issue to be decided in the case was "whether the Court over the objection of the trustee can confirm a plan which pays only a minimal dividend to unsecured creditors while the debtors continue to devote a substantial amount of their income to support of their church."<sup>261</sup> After

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promote some religious or spiritual purpose, rather than an effort to hinder, delay, or defraud creditors, and whether there is a nondiscretionary obligation to pay such expense in a specific amount. Where, as here, the obligation is nondiscretionary, the amount of such expense is not a proper subject for court scrutiny. Therefore, the sole issue here is whether the debtor's proposed tithe is intended to serve an appropriate purpose. I conclude that it is.

*Id.* (citations omitted).

258. *Id.* at 283.

259. *Navarro*, 83 Bankr. at 357. See also *In re Gaukler*, 63 Bankr. 224 (Bankr. D.N.D. 1986). In *Gaukler*, debtors with a net monthly income of \$1802.56 and four young children had a \$672 expenditure for religious giving. *Id.* at 225. The court noted that the debtors had already sold their home and moved into an apartment and had given back their automobile to the secured creditor. *Id.* Because of extreme steps to tighten the belt, the court concluded that "the Debtors are not typical of most individuals who find their way into financially destitute circumstances." *Id.* at 226. The court stated that "it seems a quite stern and uncaring religion that would require faithful adherence to such a level of giving when the persons being asked to give are jeopardizing the welfare of their family in the course of compliance." *Id.* The court held, however, that the expenditure was not unreasonable because it was a sincerely held belief and the giving was required by the church. *Id.*

260. 96 Bankr. 348 (Bankr. N.D. Fla. 1989).

261. *Id.* at 349. The debtors net monthly income was \$1,145 and they proposed to pay a 2% dividend to general unsecured creditors in their plan. *Id.* The proposed monthly expense for tithing was \$160 while their monthly payment to the plan was



noting the different approaches taken by courts in analyzing on the issue, the *Miles* court held that "while church donations may be a source of inner strength and comfort to those who feel compelled to make them, they are not necessary for the maintenance or support of the debtor or a dependent of the debtor and accordingly these debtors failed to meet the disposable income test required for confirmation of their plan."<sup>262</sup> The court rejected the constitutional argument that a court must allow tithing during a Chapter 13 plan and decided that tithing was not a reasonably necessary expense.<sup>263</sup>

### III. ANALYSIS

The courts have yet to develop a standard test to determine reasonably necessary expenses under the disposable income test of section 1325(b) of the Bankruptcy Code.<sup>264</sup> In fact, the principal problem with the disposable income test in general and the reasonably necessary expense determination in particular is that no uniformity exists.<sup>265</sup> It is not equitable that some debtors can propose more modest Chapter 13 plans strictly because of the jurisdiction in which they happen to live. Uniformity, however, does not mean that there is a formula or standard that can be applied in every situation. The fact that Congress used a "reasonably necessary" standard is an indication that any disposable income analysis will require some case-by-case scrutiny by the courts. Because the disposable income requirement is a very recent addition to the realm of bankruptcy jurisprudence, it has taken a few years for the courts to develop the issues and preliminary approaches to resolve those issues. Perhaps it is time to gather the experience gained from those early cases and develop an approach that will achieve at least three objectives: (1) maximum repayment to the unsecured creditors,<sup>266</sup> (2) uniformity and

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\$50.60 for 36 months. *Id.*

262. *Id.* at 350..

263. *Id.*

264. One court observed that "a bright line rule of what is reasonably necessary has not been established by the courts." *In re Reyes*, 106 Bankr. 155, 157 (Bankr. N.D. Ill. 1989).

265. "Congress has created a test that is so flexible in a judge's hands that it is impossible to expect any large degree of consistency between the bankruptcy courts." Comment, *Zero Payment*, *supra* note 20, at 475.

266. One court stated that "[t]he purpose of Chapter 13 is to reward the debtor who undertakes to repay his unsecured creditors with more lenient treatment than accorded a liquidation Chapter 7 debtor. (Citation omitted) '[T]he special benefits bestowed upon a Chapter 13 debtor are premised upon his willingness to repay at least some portion of his debts . . .'" *In re Strause*, 101 Bankr. 223, 224 (Bankr. S.D. Cal. 1989) (citation omitted).

predictability<sup>267</sup> among the various bankruptcy jurisdictions, and (3) rehabilitation<sup>268</sup> assistance for the debtor.

### A. Issues That Affect the Reasonableness Determination

Several issues arise in the context of determining reasonably necessary expenditures under a Chapter 13 plan that affect the approach a court uses to analyze the expenditures. Any proposed method to analyze a debtor's proposed expenditures under a Chapter 13 plan must account for these issues. First, the threshold issue is whether a bankruptcy court should have discretion to make value judgments regarding the debtor's proposed Chapter 13 lifestyle.<sup>269</sup> One commentator remarked that if a court is allowed to evaluate

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Another court criticized a Chapter 13 plan because "they have not reduced their standard of living to maximize the plan's distribution." *In re Hale*, 65 Bankr. 893, 897 (Bankr. S.E. Ga. 1988).

267. "By adding Section 1325(b)'s disposable income test, Congress intended to eliminate inconsistent judicial interpretations concerning the degree of debt that a debtor must repay to have his Chapter 13 plan confirmed." Comment, *Disposable Income*, *supra* note 55, at 221 (citing S. REP. NO. 65, 98th Cong., 1st Sess. 20, 21 (1983)). "Congress hoped to create a concrete standard which would both eliminate the disparity between the judicial districts and be consistent with the basic consumer credit theory of extending credit based on future income." *Id.* at 225. One court implied as follows that uniformity is a purpose of 11 U.S.C. § 1325(b) (1988):

Section 1325(b) can be viewed only as a floor below which no plan can go and still be confirmed, even if the general good faith test is fully met to the satisfaction of the Bankruptcy Judge. It is a 'fail-safe' mechanism to insure some uniformity in the minimum effort that will be required of debtors, even when their good faith is not questioned.

*Hale*, 65 Bankr. at 896

It can be argued, however, that uniformity and predictability are not Congressional policy objectives for bankruptcy. For example, although Congress adopted federal standards for exempt property in 11 U.S.C. § 522 (1988) of the Code, a state is allowed to establish its own exempt property guidelines and opt-out of the federal exemption. Because states are allowed to opt-out, a wide discrepancy has developed among the states regarding the amount of property a debtor may exempt from the estate. For example, some states allow a debtor to exempt his entire homestead while other states place rather low limits on the amount allowed for a homestead exemption. These varied standards in regard to exempt property resulted from Congress' decision to allow states to opt-out and apply their own standards. Thus, this situation supports the position that uniformity and predictability are not congressional goals of bankruptcy relief.

268. One court stated that "the spirit and purpose of Chapter 13 is rehabilitation through repayment of debt." *Hale*, 65 Bankr. at 894.

269. One commentator phrased the question as follows: "[a]t what point does the

the debtor's lifestyle in its determination of the reasonableness of the debtor's Chapter 13 expenditures, it "opens up a Pandora's Box of subjective and speculative value judgments of unparalleled intrusiveness."<sup>270</sup> Although some commentators oppose bankruptcy courts making judgments concerning a debtor's proposed Chapter 13 lifestyle,<sup>271</sup> bankruptcy courts must make those determinations because section 1325(b) requires<sup>272</sup> the court to make certain that all the debtor's disposable income is available for the Chapter 13 plan. Also, the courts are called upon to make the same or similar value judgments and reasonableness determinations under other sections of the Code.<sup>273</sup>

Assuming bankruptcy courts should,<sup>274</sup> and consistently do, make lifestyle determinations regarding a Chapter 13 debtor's proposed expenses, a second issue is if debtors should be allowed to maintain their prebankruptcy lifestyle. One commentator maintained that "[t]he court should not permit a

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court's review of the minutiae of a debtor's financial life become an unwarranted intrusion into personal autonomy?" Corish & Herbert, *supra* note 2, at 82. Another commentator stated that "one is forced to ask whether a court in its effort to benefit creditors, should be empowered to dictate how a debtor ought to live." Morris, *supra* note 9, at 123.

270. Breitowitz, *supra* note 3, at 352.

271. For example, one commentator remarked "'need' is hardly an objective concept and the notion that a third party will decide a family's needs is offensive to a widespread belief that such decisions be left to individuals." *Id.* at 353. Another commentator stated that "[a]lthough many individuals are in need of counselling so that they can better handle their expenses, a court should not attempt to perform this function, a task that extends well beyond its duties as an adjudicator." Gross, *supra* note 24, at 135.

One court stated as follows:

Whether a family of five should spend \$100 per month (\$25 per week) on recreation instead of paying creditors is a matter of judgment . . . . Likewise, it may be questioned whether church contributions of \$100 a month should come ahead of repayment to creditors. Having a fourth child may be a questionable luxury. At what point such inquiries and decisions by a bankruptcy court would become an affront to society's sensibilities or the U.S. Constitution remains uncertain.

*In re Edwards*, 50 Bankr. 933, 940 n.9 (Bankr. S.D.N.Y. 1985).

272. "[T]he statute [section 1325(b)] apparently requires the court to be the arbiter and architect of the defendant's [debtor's] lifestyle." Breitowitz, *supra* note 3, at 351.

273. For a good discussion of other Code provisions that require a court to determine reasonably necessary expenses, see *In re Kitson*, 65 Bankr. 615, 619 (Bankr. E.D.N.C. 1986); Corish & Herbert, *supra* note 2, at 56.

274. "A determination of the reasonableness of a debtor's expenses requires the Court to make a value judgment." *In re Ashton*, 85 Bankr. 766, 770 (Bankr. S.D. Ohio 1988).

debtor to maintain the extravagant lifestyle which may have led to the need for bankruptcy relief in the first place.<sup>275</sup> All bankruptcy courts hold that debtors should not be able to continue expenditures for luxuries during a Chapter 13 plan.<sup>276</sup> A few commentators argue that requiring debtors to reduce their pre-bankruptcy lifestyle would, contrary to congressional objectives, result in fewer Chapter 13 bankruptcies.<sup>277</sup> The trend among the courts is to examine the debtors' proposed expenditures on their own merits, rather than to compare them to the debtors' pre-bankruptcy lifestyle.<sup>278</sup> The courts disfavor allowing debtors to upgrade their living expenditures under a

275. Morris, *supra* note 9, at 158.

276. One court stated in reference to a debtor who sought to retain a Rolex watch in his Chapter 13 plan as follows:

If a debtor cannot pay his bills as they become due, and seeks the protection of the bankruptcy court, he is not required to forego all physical and social pleasures. Neither is he to don sackcloth and ashes and proclaim his misfortune to the world as past day lepers were required to do. Nevertheless he is constrained to live somewhat more modestly than to the style that led to his fall from financial grace. It does not take a multi-thousand dollar device to discern the precise moment of the day or night - a comparable result can be obtained by a much less expensive means.

*In re Holcomb*, Case No. 88-00535-W-13 (Bankr. W.D. Mo. 1988) (Unpublished opinion of Koger, J.).

277. For example, one commentator stated as follows:

Obviously, those high income debtors would be discouraged from filing chapter 13 if they were forced to trim their lifestyles too severely. If BAFJA were interpreted in a way that led to fewer reorganizations, rather than more, its purposes presumably would be frustrated. Of course, this problem could be alleviated by the vigorous use of Section 707(b) to force reorganization. Thus, if the courts do in time adopt a more stringent definition of permissible lifestyle expenses, they will also have to monitor petitions more closely for signs of substantial abuse.

Corish & Herbert, *supra* note 2, at 74.

The same commentator noted that "at least one early study of the disposable income standard expressed concern that, by increasing the cost of a Chapter 13 discharge, Congress had discouraged consumer Chapter 13 proceedings." *Id.* at 78 (citation omitted). The commentator went on to note, however, that "[a]lthough the available statistics are rather spotty, this does not appear to be the case. Chapter 13 proceedings appear to be about as popular now as they were before BAFJA." *Id.*

278. One commentator stated in reference to another Code section that requires a determination of reasonably necessary expenses that "[c]ourts which have considered the debtor's reasonable needs for the purposes of section 522(d) generally have suggested that the debtor's prebankruptcy lifestyle does not limit the court's postbankruptcy determination of reasonableness." Morris, *supra* note 9, at 157-58 (citations omitted).

Chapter 13 plan; but most bankruptcy courts would not take the position that debtors may never add to a Chapter 13 plan any expense that the debtors were not expending pre-bankruptcy.

A third issue is the criteria that a bankruptcy court uses to evaluate the proposed expenditures in a Chapter 13 plan. The courts must evaluate the expenditures according to some standards. Should the courts compare the debtor's proposed expenditures to those of other debtors or to some average amounts for the area? Should the standards be objective? Commentators have debated whether bankruptcy courts should use objective standards to reduce a Chapter 13 debtor's expenditures to uniform levels.<sup>279</sup> Neither the Code nor the legislative history of section 1325(b) establishes any objective standards.<sup>280</sup> Currently, there is no indication in the case law that any bankruptcy jurisdiction is using objective criteria as a measuring stick to determine reasonably necessary expenses.<sup>281</sup> The courts and most commen-

279. For example, one commentator stated that "courts should not be in the business of equalizing all debtors to the same social standard on the basis of the court's own predilections of how people in financial trouble ought to live." Gross, *supra* note 24, at 132. The same commentator reasoned that:

If courts do not intervene with respect to a debtor's expenditures, creditors will be forced to make a more careful evaluation of the risks of lending to a particular individual. Rather than making the court a collection agency, creditors ought to do a better job of evaluating credit risks, with the consequence of an error in that process falling on the creditors rather than the debtor. This shift in risk allocation makes sense from an economic perspective. Creditors are in the best position to judge the ability of an individual to repay.

*Id.* at 134.

Another commentator stated, however, that "the problem created by permitting Chapter 13 debtors to enjoy very different lifestyles based on their social and economic status should at least be addressed by the courts." Corish & Herbert, *supra* note 2, at 74. The same commentator asked "to what extent is it fair to permit a high-income debtor to retain an approximately upper-middle class lifestyle," and then stated that the problem "could have been alleviated by the imposition of a more objective standard." *Id.* at 82.

280. "Congress gave no indication of what types of expenses were reasonably necessary. Congress set up a standard which vests large discretion in judges and then provided no guidelines to assist in creating uniformity." Comment, *Zero Payment*, *supra* note 20, at 463-64.

281. "The courts have generally followed an unobjectionable commonsensical approach to lifestyle expenses, neither requiring asceticism nor condoning hedonism." Corish & Herbert, *supra* note 2, at 71. "The disposable income cases have permitted the debtor to continue something resembling his prior lifestyle. The debtor has not been forced to live in bankruptcy poverty, or anywhere near bankruptcy poverty, unless he was already poor." *Id.* at 73 (citations omitted). "While the 'collection' oriented

tators maintain that a case-by-case analysis of proposed Chapter 13 expenditures is the method intended by Congress and a logical requirement for a reasonably necessary test.<sup>282</sup> State garnishment laws, however, are an example of objective criteria applied to an overextended debtor. Under state garnishment laws, only a certain percentage of a debtor's wages is available for attachment by judgment creditors.<sup>283</sup> Thus, there is precedent for

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courts are capable of harsh rhetoric, the bottom-line differences between acceptable and unacceptable plans are relatively modest." *Id.* at 80. "In part the popularity of Chapter 13 is due to the wide discretion which the courts have exercised in applying the standard [§ 1325(b)]; despite protestations to the contrary, this discretion has generally been exercised in favor of permitting the debtor to maintain some semblance of his prior lifestyle. *Id.* at 82.

282. The premise of these advocates is that by using the "reasonably necessary" standard, Congress intended to give no guidance and to leave the determination up to the courts. In other words, determining "reasonableness" requires discretion. One commentator stated that:

Each case should be handled by application of a flexible standard that recognizes the debtor's freedom to determine at least the contours of how she lives while according the court some discretion in balancing that freedom with the rights of creditors to be repaid. Applying a uniform standard of how debtors should live, whether based on a court's subjective assessment or a fixed federal standard creates, in essence, a class of bankruptcy poor. A case-by-case approach frees both the debtor and the court by permitting the court to blend both an objective and subjective component into its decisionmaking process.

Gross, *supra* note 24, at 133.

283. For example, the Bankruptcy Court for the Western District of Missouri noted that "Missouri state law effectively exempts from garnishment all but 25% of an individual's earnings and all but 10% of those earnings if the individual is the head of a family and is a resident of Missouri." *In re Antal*, 85 Bankr. 838, 840 (Bankr. W.D. Mo. 1988) (citing MO. REV. STAT. § 525.030(2) (1986)).

One commentator discussed garnishment laws as follows:

For example, in determining what portion of a debtor's wages should be garnished, state courts have looked at what amount a debtor needs to support herself and her family and in some instances have precluded garnishment of these amounts. Recognizing the difficulties inherent in such determinations, most garnishment statutes now permit garnishment based on a percentage of total income, thereby eliminating or minimizing the need for subjective evaluations of expenditures.

Gross, *supra* note 24, at 123-124 (citations omitted).

Furthermore, "the Federal Government has put a ceiling on the amount above which the state garnishment statutes may not exceed. Generally, the ceiling is 25% of the individual's disposable weekly income, with exceptions for court-ordered spousal or child support payments." See 15 U.S.C. § 1673 (1982); Gross, *supra* note 24, at 124 n.278:

establishing objective standards for evaluating the reasonableness of a Chapter 13 debtor's proposed expenditures.

Two final issues are more related to policy than to the mechanics of the reasonableness determination. First, does the disposable income test operate as a disincentive for the debtor to minimize expenditures in the Chapter 13 plan<sup>284</sup> and to encourage debtors to schedule discretionary expenditures during the plan.<sup>285</sup> Any belt-tightening on expenses by the Chapter 13 debtor increases the dividend to general unsecured creditors. Thus, the benefit from reducing expenditures accrues to the creditors, not the debtor. Therefore, if debtors have been delaying an expenditure due to a lack of funds, they can potentially pay for it under their Chapter 13 plan at no additional cost by proposing it as a reasonably necessary expense. For example, one commentator hypothesized that "the debtor's child might need orthodontic work, which the debtor has been delaying because he does not want to spend the money. Since that money will go to creditors if it is not used to fix the child's teeth, it literally costs the debtor nothing to have the work done during the plan period."<sup>286</sup> Second, an issue exists as to whether a debtor's dependents should be forced to make sacrifices under the debtor's Chapter 13 plan. For example, should a debtor's children be forced to forgo piano lessons during a Chapter 13 plan? The case law does not directly address these two issues. They are policy issues, however, that permeate Chapter 13 plans and directly affect the results from jurisdiction to jurisdiction.

### *B. Summary Principles From The Case Law*

The case law illustrates there are differences in treatment among the various categories of expenditures under a Chapter 13 plan, and problems are unique to each category. Housing expenditures present distinct policy issues. Any disposable income analysis must consider the Chapter 13 policy objective for debtors to be able to retain their home. Absent an obviously excessive expenditure, the debtor should be allowed to continue in the same residence. The court should determine, however, whether the debtor is living in an

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284. "Just as the disposable income standard reduces the debtor's incentive to earn, so too it reduces the debtor's incentive to minimize expenses." Corish & Herbert, *supra* note 2, at 72.

285. "To what extent can the debtor voluntarily increase his 'reasonably necessary' expenses during the plan period?" *Id.*

286. *Id.* The same commentator, however, stated that "[t]here is little indication in the cases that this has been much of a problem." *Id.* The commentator speculated that this could be because creditors are not adept at spotting these discretionary expenditures on the debtor's schedules. *Id.*

unaffordable area or home based on the debtor's level of income.<sup>287</sup> The ultimate question is whether the debtor purchased a home that stretched his or her budget beyond its limits. If so, the court should require the debtor to move to a less expensive home before it will confirm the debtor's Chapter 13 plan.<sup>288</sup> This approach would help the debtor make expenditure changes that will enhance the debtor's financial stability long after the plan has ended. A second consideration is whether the debtor is using Chapter 13 to upgrade housing at the expense of general unsecured creditors. The court should determine if the debtor acquired the residence just before filing the bankruptcy petition to make less disposable income available for the Chapter 13 plan. Once again, if the answer is yes, the court should require the debtor to move to more affordable housing as a requisite to plan confirmation.

The courts historically have used the most subjective criteria, and produced the most varied results, when determining the reasonableness of a debtor's expenditures for transportation, food, clothing, and recreation. The reasonableness determination for these expenditures could be made with reference to objective standards. The courts could establish average cost of living standards for their particular geographical area. For example, the debtor's proposed expenditures for transportation and food could be compared to average monthly costs for the area. Expenditures for clothing and recreation could be analyzed with reference to established standards based on a percentage of net income. This approach would account for differences in cost of living and would allow the debtor reasonable expenditures commensurate with averages for the area.

The most difficult reasonableness determinations for the courts in a Chapter 13 plan are the expenditures for religious and charitable giving and parochial and private school education. As discussed *supra* in Sections II. F. and II.H. of this Comment, these expenditures present the courts with complex and difficult social, constitutional, and religious policy considerations. One approach suggested in the cases, however, would examine the debtor's past

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287. See, e.g., *In re Rice*, 72 Bankr. 311, 312 (D. Del. 1987) (the court found that the debtors would have been able to make greater payments to their plan had they sold their expensive home and purchased a more reasonable home for their income level).

288. *Id.* The court held that the debtors ability to make greater payments to their plan would "require adjustments on their part which are greater than keeping their new house at the expense of their unsecured creditors." *Id.*

One commentator stated as follows:

[i]n most cases, a monthly rental or mortgage payment is the largest single expenditure in the debtor's budget. If other directly related expenses are included, such as utility costs and taxes, the expense grows even larger. If the debtor resides in large or lavish quarters, the court might feel compelled by section 1325(b)(1)(B) to withhold confirmation of the debtor's plan until the debtor moves to less expensive quarters. Morris, *supra* note 9, at 158.



behavior to ascertain sincere belief and commitment before filing for Chapter 13. Thus, if the debtor had always contributed to a religious or charitable organization, or had made parochial or private education a priority, those expenditures could continue at the same or some reduced level.

### C. Suggestions for Debtors and Creditors

Based on an analysis of case law interpreting reasonable expenses under the disposable income test, debtors and their attorneys can follow some overall guidelines that should improve their chances for plan confirmation. *First*, the debtor should submit an initial Chapter 13 plan that is credible and that actually reflects the debtor's reasonably necessary living expenses. It is not an advantageous tactic for a debtor to submit an inflated budget with the anticipation that he can negotiate the expenses downward if challenged by the trustee or an unsecured creditor.<sup>289</sup> The courts are skeptical of debtor credibility when inflated original budgets are replaced by more realistic budgets, and the courts tend to scrutinize the resubmitted budget to a greater degree. *Second*, the debtor can be reasonably confident that housing and transportation expenses will be allowed unless they are obviously excessive. Thus, the debtor should consider proposing to sell a luxury car as a part of the plan. *Third*, debtors should be very conservative on proposed recreational expenditures. One commentator advised that "considering the potential for creditor outrage, debtor's attorneys would be well advised to closely examine all recreational expenses for reasonableness."<sup>290</sup> *Fourth*, if debtors intend to include charitable giving, tithing, or private school education expenditures in the Chapter 13 plan, they should (1) consider whether they have a credible history of religious or charitable conviction, (2) limit the amounts to a reasonable level, and (3) consider proposing a plan longer than three years in duration.<sup>291</sup> If debtors have delayed a discretionary expenditure due to a lack of funds, they may want to consider proposing it in the plan.<sup>292</sup> These

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289. "Counsel for debtors should perceive that required schedules are not to be given short shrift in filing a petition for relief, even in a simple Chapter 7 case. Instead they should analyze what the real expenses of living in today's world are and seek to memorialize them in their initial filing." *In re Campbell*, 63 Bankr. 702, 706 (Bankr. W.D. Mo. 1986).

290. Butler, *supra* note 10, at 413.

291. One commentator suggested in regard to proposed religious or charitable contribution expenditures that "[a] debtor wishing to continue such contributions might consider extending the plan beyond 36 months to satisfy an objecting creditor." *Id.* at 412-13. See *infra* notes 301-309 and accompanying text for a discussion of the issues raised when a debtor extends a Chapter 13 plan past three years.

292. See *supra* notes 278-279 and accompanying text for a discussion of proposing discretionary expenses in the plan.

expenditures, however, would need to be reasonably necessary expenses for support and maintenance. *Fifth*, any proposed contingency fund for emergencies should be included in the plan as a contingency fund rather than as a savings account.

Creditors can act in regard to an individual debtor plan or towards changes in the Chapter 13 provisions in general. *First*, creditors should become more active in objecting to Chapter 13 plans when they believe some expenditures are unreasonable.<sup>293</sup> Commentators have suggested that creditors do not actively object to Chapter 13 expenditures because the amounts involved are not significant enough.<sup>294</sup> Creditors cannot complain, however, about excessive expenditures in Chapter 13 plans if they fail to object. *Second*, creditors should develop objective guidelines for determining reasonably necessary expenses and work to have them adopted by their local bankruptcy court and Congress.<sup>295</sup> Because creditors extend credit based on their credit analysis of the debtor's current expenditures and future income, the creditors are in the best position to suggest objective guidelines for the courts to follow in determining reasonably necessary expenses.<sup>296</sup> For example, creditors could create dollars-per-month or percent-of-net-income criteria as models for the courts to use in their geographic area.

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293. One commentator observed that "creditors do not seem to file many objections to Chapter 13 plans." Corish & Herbert, *supra* note 2, at 79.

294. "The amounts of money involved in the typical Chapter 13 case discourage much creditor activity and have led to the present system in which creditor participation is reduced to a minimum." *Id.*

295. A commentator observed that

Curiously, it appears that no major creditor has attempted to mitigate this cost—and make objections economically feasible—by creating hypothetical 'disposable income profiles' for debtors. It would be quite easy for a major lender to develop such profiles from their own credit scoring systems. Since those systems are used to measure ability to pay before the loan is made, they could also be used to measure ability to pay after Chapter 13 is filed . . . Moreover, if courts came to accept such profiles as a baseline for measuring disposable income, the need for objections would diminish as debtor's lawyers learned to draft plans that initially conformed to the profiles.

Corish & Herbert, *supra* note 2, at 79.

296. One commentator stated that an "[i]ndustry spokesman noted that a debtor's anticipated future income was the primary consideration in making consumer loans." Morris, *supra* note 9, at 94 (citation omitted).

### D. Weaknesses of Current Approaches

Historically, each of the approaches used by the courts to evaluate if a debtor's expenses are reasonably necessary under a Chapter 13 plan suffers from identifiable weaknesses. The narrow interpretation of disposable income under which the court seeks only to remove "luxury" amounts from the debtor's proposed plan is too limited. If a court only requires a debtor to reduce expenditures on obvious luxury items, the debtor could upgrade his basic lifestyle at the expense of his general unsecured creditors. Certainly, the court should scrutinize a budget for obvious luxuries because "Chapter 13 debtors should not be able to continue the extravagances which put them into bankruptcy, while their unsecured creditors go unpaid."<sup>297</sup> Thus, although it is limited, the luxury expenditure test should remain as a baseline requirement for disposable income.

On the other hand, the broad interpretation that seeks to reduce all debtors to a very basic lifestyle lacks flexibility. Should debtors with different income levels be required to live at the same expense level? Unsecured creditors should not be allowed to cry "foul" when they could reasonably expect a certain level of expenditures based on a borrower's income level. After all, they extended the credit based on that income level. Also, this approach raises the issue as to whose values should be used to determine lifestyle for a debtor at a particular income level.<sup>298</sup>

The most feasible approach among the historical approaches to the disposable income analysis may be the "totality of the circumstances" approach. Under this approach, the court considers each Chapter 13 plan on its own merits and analyzes the expenditures as a whole. This approach allows flexibility for the court and a more equitable determination of the total picture. One drawback of this approach, however, is the lack of objective guidelines for the court to follow and an absence of emphasis on the objectives of maximizing the unsecured creditor dividend and rehabilitating the debtor.

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297. *In re Reyes*, 106 Bankr. 155, 157 (Bankr. N.D. Ill. 1988). See also *In re Sutliff*, 79 Bankr. 151, 157 (Bankr. N.D.N.Y. 1987) ("Debtors should not be allowed to continue in the lifestyle that drove them to file bankruptcy and at the expense of their creditors.").

298. The problem is that "an inquiry into a debtor's 'reasonably necessary' expenses is unavoidably a judgment of values and lifestyles and close questions emerge." *In re Sutliff*, 79 Bankr. 151, 156 (Bankr. N.D.N.Y. 1987).

### *E. An Alternative Approach*

Based on the foregoing analysis, an alternative approach for determining reasonably necessary expenses can be developed by combining the suggestions developed in the Case Law section of this Comment. Any approach should operate to achieve the three objectives listed at the beginning of this section: (1) maximum repayment to the unsecured creditors, (2) uniformity and predictability among the various bankruptcy jurisdictions, and (3) rehabilitation assistance for the debtor. These goals will require a test that limits the debtor's expenditures according to specific and defined standards. It is important to remember that requiring a debtor to adjust spending habits is essential to the debtor's continued financial success after completion of the Chapter 13 plan. The following is a suggested method of analysis for proposed expenditures in a Chapter 13 Plan.

#### 1. Eliminate Luxury Expenditures

As a threshold inquiry, the court should determine if a proposed Chapter 13 expenditure is a reasonable expenditure. This initial inquiry is not concerned with a proposed amount, but rather with a proposed expense. The court in this step is simply eliminating luxury items from the debtor's Chapter 13 expenditures, such as a luxury boat<sup>299</sup> or motor home.<sup>300</sup>

#### 2. Evaluate Expenditures According To Objective Standards

For expenditures deemed reasonable, the court should evaluate the debtor's proposed Chapter 13 expenditure amounts according to an established set of objective criteria. These measuring criteria should be established for each expenditure category and for the Chapter 13 plan as a whole. For example, standards for specific categories could approximate the following:

(a) Housing: If the debtor is making mortgage payments, the payments should be allowed unless they are excessive in relation to the debtor's income or the debtor is using Chapter 13 to upgrade his housing. The court could use an established standard based on a percentage of net income to evaluate reasonableness, such as twenty-five percent of net income. A proposed expenditure for a home mortgage payment below that level would be presumed reasonable. If the debtor is renting a home or apartment, a similar standard could be established that is related to net income and family size. Each jurisdiction would need to establish average rental amounts for its geographic area.

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299. *In re Hedges*, 68 Bankr. 18 (Bankr. E.D. Va. 1986).

300. *In re Struggs*, 71 Bankr. 96, 98 (Bankr. E.D. Mich. 1987).

(b) Expenditures for food, transportation, clothing, recreation, and contingency needs should also be measured according to an objective standard. Food and recreation expenses could be compared to established criteria based on per-person amounts. For example, each jurisdiction could develop tables that would delineate allowable expenditures for each category based on costs of living for the geographic area with consideration given to family size and ages of dependents. Expenditures for transportation and clothing could be based on a percentage-of-net income standard. Expenditures for all these expense categories that were within the established criteria would be presumed reasonable.

(c) Expenditures for charitable giving and private school education should be discontinued during the course of the plan. An exception could be allowed for religious contributions and parochial school education. Religious contributions and parochial education expenditures, however, would be allowed only if the debtor established a sincere commitment based on past behavior. An alternative standard for these expenditures would allow them within a certain maximum percentage of net income. For example, the debtor could propose contribution expenditures amounting to less than three percent of net income.

(d) An additional standard should be established for total expenditures. Under this standard, the debtor's proposed expenditures could not exceed a specified percentage of net income. For example, seventy-five percent (75%) could be established as the standard. The debtor's total proposed expenditures could not exceed seventy-five percent of the debtor's net income. This standard could be used either as an overall check for the individual categories, or as the only standard for the debtor's expenditures. If used as the latter, the court would not evaluate each expense category under established standards, but would only evaluate the debtor's total expenditures based on this total-expenditure standard. Thus, the debtor would be allowed any amount of expenditure in any specific category and the only limitation would be the total expenditures.

### 3. Allow Court Discretion for Compelling Circumstances

Any approach to evaluating proposed expenditures needs to allow for judicial discretion based on compelling circumstances in a specific case. It would be unrealistic to assume that a set of objective criteria could equitably account for every possible situation. For example, the court could use its discretion to allow greater amounts of expenditures when a debtor or a dependent had burdensome health expenditures. The court's discretion, however, should be limited to compelling circumstances. Otherwise, the goals of predictability and uniformity would be effectively undermined.

#### 4. Allow Voluntary Extensions of the Plan Length

Under section 1322(c) of the Code,<sup>301</sup> the debtor's Chapter 13 plan cannot exceed 36 months in length without a showing of cause. It is unsettled whether a debtor's desire to increase the dividend to general unsecured creditors is sufficient cause to allow extension of a Chapter 13 plan beyond 36 months.<sup>302</sup> Many courts, however, allow the debtor to voluntarily extend

301. Section 1322(c) reads in full:

(c) The plan may not provide for payments over a period that is longer than three years, unless the court, for cause, approves a longer period, but the court may not approve a period that is longer than five years.

11 U.S.C. § 1322(c) (1988).

302. There is a split among the bankruptcy courts as to whether a desire by the debtor to pay a greater dividend to unsecured creditors is sufficient cause for the court to confirm a plan that is longer than three years in duration. Some courts take the position that it is not sufficient cause. For example, one court held that "a debtor's desire to increase the dividend paid to general unsecured creditors, without more, does not rise to the required level for exceeding the prescribed 36 month period." *In re Festa*, 65 Bankr. 85, 86 (Bankr. S.D. Ohio 1986). The court reasoned that "such extensions would become routine and would emasculate the statutory preference for 36 month plans." *Id.* at 87. Another court reasoned that Congress prescribed three-year plans because of concerns about involuntary servitude if plans went beyond three years. *In re Greer*, 60 Bankr. 547, 555 (Bankr. C.D. Cal. 1986). The court held that a desire to pay at least a 70% dividend to general unsecured creditors would be sufficient cause for extending a plan past three years because, under § 727(a)(9) of the Code, a 70% dividend would allow the debtor to receive a Chapter 7 discharge without having to meet the prescribed six year limitation. *Id.* See also *In re Karayan*, 82 Bankr. 541, 542-43 (Bankr. C.D. Cal. 1988) (the court noted three situations in which extensions are approved: (1) when the debtor proposes to pay a 100% dividend to unsecured creditors in order to enhance his credit rating, (2) when the debtor desires to pay at least a 70% dividend to eliminate the applicability of § 727(a)(9), and (3) when the debtor is allowed to suspend post-confirmation plan payments); *In re Wood*, 92 Bankr. 264, 266 (Bankr. S.D. Ohio 1988); *In re Frank*, 69 Bankr. 129 (Bankr. C.D. Ill. 1986).

Other courts, however, have held that a debtor's desire to increase the dividend to unsecured creditors in his Chapter 13 plan is sufficient cause to approve a plan longer than three years. One court distinguished *Greer* by noting that, in those cases, the debtor did not propose a plan longer than three years and it was the creditors or trustee who were requesting the plan extension. *In re Pierce*, 82 Bankr. 874, 883 (Bankr. S.D. Ohio 1987). The court concluded that a voluntary plan extension by the debtor would be sufficient cause to extend the plan. *Id.* at 885. Another court interpreted the debtor's unwillingness to propose a five-year plan as a lack of a good faith effort to repay unsecured creditors. *In re Swan*, 98 Bankr. 502 (Bankr. D. Neb. 1989). Although the court indicated it could not force the debtor to extend his plan past three years, it refused to confirm the debtor's three year plan because of a lack

their plan up to the five-year maximum. Thus, one alternative for courts to allow the debtor more spending discretion under this objective-standards approach is to allow the debtor to increase expenditures in the Chapter 13 plan if the debtor proposed to increase the length of the plan.

In an unpublished opinion, *In re Ivy*,<sup>303</sup> the Ninth Circuit implied that voluntary plan extension could be an alternative for debtors who desired to include in their Chapter 13 plan an expenditure amount that was not reasonably necessary. In *Ivy*, the debtors proposed to tithe to their church in a Chapter 13 plan that was 36 months in length with a twenty-seven percent dividend to unsecured creditors.<sup>304</sup> The bankruptcy court refused to confirm the plan because the religious contribution was not a reasonably necessary expense.<sup>305</sup> The bankruptcy court, however, gave the debtors the option to include the tithe and extend the plan an additional eighteen months.<sup>306</sup> The debtors refused to extend their plan and appealed the ruling on constitutional grounds.<sup>307</sup> The Ninth Circuit stated that it was not necessary to decide the constitutional issues because the debtors refused to accept the reasonable alternative of extending their plan.<sup>308</sup> The court stated that "in rejecting the amended plan, the Ivy's instead sought to choose accommodation of their religious beliefs at the expense of their creditors. We decline to hold that this

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of good faith. *Id.* at 504. See also *In re Little*, 116 Bankr. 615, 621 (Bankr. S.D. Ohio 1990) ("where, as in the present case, the debtor desires to repay a higher percentage of her debts the three-year period can be extended, at the debtor's request and with the court's permission, to as long as five years."); *In re Hale*, 65 Bankr. 893, 896 (Bankr. S.D. Ga. 1988) (the court, in analyzing a proposed Chapter 13 plan for good faith, criticized the debtor for not proposing a plan longer than three years "as they are permitted to do.").

For a thorough discussion of the issues related to extending a Chapter 13 plan beyond three years for cause, see Comment, *Chapter 13: "Cause" for Extension Under Section 1322(c)*, 5 BANKR. DEV. J. 249 (1987).

303. No. 88-3769 (9th Cir. (Or.) Dec. 10, 1990) (WESTLAW, Allfeds database).

304. *Id.* at 2.

305. *Id.* "The court found that the plan's exclusion of the tithe from the amount of disposable income payable to the Ivy's creditors would effectively require the creditors to contribute to the Ivy's chosen charity." *Id.*

306. *Id.* The court calculated that the extra eighteen months would produce the same dividend to the general unsecured creditors under the extended plan as a 36 month plan without the expenditures for the tithe would have produced. *Id.*

307. *Id.* at 1. The debtors maintained that the bankruptcy court violated their constitutional right to free exercise of their religion under the Establishment Clause of the First Amendment of the United States Constitution. *Id.* For a discussion of this constitutional issue, see *supra* notes 237-263 and accompanying text.

308. *Id.*

satisfies the Code's requirements.<sup>309</sup> Thus, by proposing a plan beyond 36 months, a debtor would commit more payment to the plan and could be allowed a corresponding increase in unnecessary expenditures. This option would allow debtors to spend more than is reasonably necessary, while at the same time maintain the same dividend to general unsecured creditors.

#### IV. CONCLUSION

The determination of reasonably necessary expenses for a Chapter 13 debtor is a very complex issue because of competing policy objectives: attempting to give the debtor a fresh start on the one hand and attempting to repay creditors to the greatest possible extent on the other.<sup>310</sup> The determination is a balancing test for courts because debtors and creditors take a different view of what constitutes reasonably necessary expenses.<sup>311</sup> Any attempt to analyze or establish acceptable levels of plan expenditures, however, must be made with a view toward accomplishing the threefold objective of a Chapter 13 plan. First, most courts and commentators acknowledge that a plan should seek to maximize the dividend to unsecured

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309. *Id.*

310. One court stated the competing goals as:

This Court believes that a debtor should not be permitted to indulge in luxury expenses during the course of his Chapter 13 plan at the expense of his creditors. The debtor is entitled to a fresh start, but he is not entitled to 'lead the life of Riley' . . . . In this Court's opinion, luxury expenses are not reasonable expenses necessary for the debtor's support. On the other hand, a debtor does not have to dedicate his last cent to his creditors; but is entitled to properly support himself and his dependents in a reasonable fashion.

*In re Ashton*, 85 Bankr. 766, 770 (Bankr. S.D. Ohio 1988) (citations omitted).

311. One commentator stated in regard to Congressional adoption of 11 U.S.C. § 1325(b) (1988) of the Code that:

Creditors argued that Chapter 13 debtors should reduce or eliminate entertainment and other nonessential expenses. Representatives of debtor interests, however, asserted that debtors should not have to live in poverty before they may qualify for Chapter 13 relief. By adopting the ability-to-pay test, Congress responded to both of these demands. On the one hand, debtors cannot continue to spend at a level above what is reasonably necessary to support themselves and their dependents. Because Congress primarily aimed the BAFJA consumer bankruptcy amendments at the excessive spender, the debtor 'cannot expect to 'go first class' when 'coach' is available.' On the other hand, the ability-to-pay test's 'reasonably necessary' standard provides enough cushion to ensure that a Chapter 13 debtor will not live in poverty.

Comment, *Religious Debtor's*, *supra* note 29, at 881 (citations omitted).



creditors.<sup>312</sup> Second, a few courts recognize there should be some uniformity to the system.<sup>313</sup> Most courts and commentators, however, forget that one of the major objectives of a Chapter 13 plan should be the rehabilitation<sup>314</sup> of the debtor. Here, the courts should focus on rehabilitation, not retribution. After all, what is accomplished if a Chapter 13 plan allows the debtor to maintain spending habits that will almost certainly guarantee continued problems after the plan is completed? Belt-tightening measures should be implemented to help debtors live within their income and assure financial success well into the future. Belt-tightening in a retributory fashion that results in failure of the plan, however, is not beneficial to anyone. The

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312. One court stated that the purpose of the disposable income standard of 11 U.S.C. § 1325(b) (1988) is to ensure that debtors "are sincerely trying to repay all their creditors to the best of their ability." *In re Compton*, 88 Bankr. 166, 168 (Bankr. S.D. Ohio 1988).

313. "One purpose of the enactment of 11 U.S.C. § 1325(b) is to create a benchmark for judging debtors' efforts in cases where the trustee or unsecured creditors believe that debtors are not making their best effort to repay creditors and are therefore abusing the bankruptcy process." *In re Tracey*, 66 Bankr. 63, 66 (Bankr. D. Colo. 1986).

314. *See supra* note 268 and accompanying text.

overriding goal should be a plan that the debtor can complete, because successful Chapter 13 plans are necessary to maintain debtor and creditor confidence in the reorganization system.<sup>315</sup>

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315. The Honorable Judith A Boulden, United States Bankruptcy Judge for the District of Utah authored an appendix to *In re Reyes*, 106 Bankr. 155, 159-61 (Bankr. N.D. Ill. 1989). She stated the following:

The success of Chapter 13 encompasses a value to the system that is larger than the sum total of the successful Chapter 13's that have been confirmed and consummated. That value is in establishing and maintaining the credibility of the Chapter 13 system. That credibility generates creditor confidence that Chapter 13's are successful, will fairly repay money to them, can be counted upon to be administered promptly and equitably, and provide the positive rehabilitation desired in bankruptcy. If the credibility of the Chapter 13 system generates creditor cooperation and encouragement, debtors will find their plans more economically and expeditiously confirmed, thus enabling debtors to receive their discharges sooner.

*Id.* at 160.

She stated that when debtors are unable to complete their plans, "it only serves to undermine the confidence that creditors have in the system. Repetitive filings, low repayment plans, attempts to retain expensive consumer items, or liberal budgets, only to [sic] serve destroy the credibility of Chapter 13 as an equitable means of repayment and rehabilitation." *Id.* at 161. Further, the Judge believes that "the integrity and credibility of the system is dependent in large upon Chapter 13 debtors consummating plans which repay the maximum amount possible to creditors." *Id.* at 160. Therefore, she stated that a debtor must have a "commitment and desire to repay creditors over an extended period of time," and that "a plan should not be confirmed when it is apparent that the sole intent of the debtor is to retain assets, not to repay creditors." *Id.* at 160-61. In fact, the Judge went so far as to state that "I believe Chapter 13 was intended for a relatively select group of individuals." *Id.* at 160.

